COURT OF APPEALS OF NEW YORK

No. 138, No. 139

In the Matter of Orvis Company Inc., Respondent-Appellant, v. Tax Appeals Tribunal of the State of New York et al., Respondents, Commissioner of the New York State Department of Taxation and Finance, Appellant-Respondent.

In the Matter of Vermont Information Processing Inc., Respondent, v. Tax Appeals Tribunal of the State of New York, Respondent, Commissioner of Taxation and Finance of the State of New York, Appellant.

Orvis Co. v. Tax Appeals Tribunal of the State of New York

June 14, 1995, Decided

No. 138: Opinion by Judge Levine. Chief Judge Kaye and Judges Simons, Titone and Smith concur. Judge Bellacosa dissents and votes to affirm in a writing in which Judge Ciparick concurs.

No. 139: Opinion by Judge Levine. Chief Judge Kaye and Judges Simons, Titone and Smith concur. Judge Bellacosa dissents and votes to affirm in an opinion in which Judge Ciparick concurs.

LEVINE, J.:

On these appeals, the State Commissioner of Taxation and Finance seeks to overturn two decisions of the Appellate Division[1] holding that Vermont vendors of products purchased by New Yorkers for use in this State were immunized from the duty

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[1] *Matter of Orvis Co. v Tax Appeals Tribunal of State of N.Y.*, 204 AD2d 916; *Matter of Vermont Information Processing, Inc. v Tax Appeals Tribunal of State of N.Y.*, 206 AD2d 764.

to collect State compensating use taxes (Tax Law § 1110) under the Commerce Clause (US Const, Art I, § 8) of the Federal Constitution. Petitioner Orvis Company, Inc. (Orvis) sells, at both retail and wholesale, camping, fishing and hunting equipment, casual and outdoor clothing and food and various gift items. Orvis' retail sales were almost entirely through mail-order catalog purchases shipped from Vermont by common carrier or the United States mail. Orvis also sold merchandise at wholesale to New York retail establishments. Concededly, Orvis employees visited New York retailers to whom it sold merchandise during the three year audit period.

Relying upon *Quill Corp. v North Dakota* (504 U.S. 298, 112 S Ct 1904), the Appellate Division held that in the absence of a substantial physical presence by Orvis personnel in New York, the imposition of the duty to collect use taxes from its New York mail-order purchasers contravened the Commerce Clause. The Court concluded that Orvis' "sporadic activities in New York" failed to meet the substantial physical presence standard and, therefore, the assessment of the tax was invalid (204 AD2d, at 918).

Petitioner Vermont Information Processing, Inc. (VIP) markets computer software and hardware to beverage distributors in New York and elsewhere throughout the United States. In most instances, its customers' orders were filled through shipments by common carrier or United States mail. An audit of VIP's invoices and sales records, however, showed visits by its employees to New York customers to resolve problems and give additional instructions in connection with the use of VIP software programs, and occasionally for installing software. The Appellate Division again concluded that those activities were insufficient to constitute the requisite substantial physical presence of VIP in this State and annulled the determination assessing the tax.

We do not read *Quill Corp. v North Dakota* to make a *substantial* physical presence of an out-of-State vendor in New York a prerequisite to imposing the duty upon the vendor to

collect the use tax from its New York clientele. The Appellate Division erroneously applied that exacting standard in both cases.

I.

The true holding of *Quill Corp. v North Dakota* can best be understood by considering the case in the context of its position in the evolution of Supreme Court doctrine limiting the authority of a State to assess or impose a duty to collect taxes arising out of the economic activity of a foreign business engaged in interstate commerce. The constitutional limitations on such authority have been derived from two sources. The first is the Due Process Clause of the Fourteenth Amendment, pertaining to the jurisdiction to tax, or the "taxing power", of a State (*Wisconsin v J.C. Penney*, 311 U.S. 435, 445). The second source is the so-called "dormant" or "negative Commerce Clause, by virtue of which the constitutional grant of power to Congress "to regulate commerce * * * among the several states" (US Const, Art I, § 8, cl 3) has been interpreted as implicitly prohibiting, even in the absence of Congressional regulation, unduly burdensome or discriminatory State taxation of transactions or entities engaged in interstate commerce (see, *Oklahoma Tax Commn. v Jefferson Lines, Inc.*, 514 U.S. ____, ___, 115 S. Ct. 1331, 1335-1336 [Apr. 3, 1995]; *Quill Corp. v North Dakota, supra*, 504 US, at ____; 112 S Ct, at 1911).

Under its Due Process clause analysis, the Supreme Court has fashioned a requirement that, for a State to validly tax an interstate commercial activity, there must be "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax" (*Miller Bros. Co. v Maryland*, 347 U.S. 340, 344-345; *see, Moorman Mfg. Co. v Bair*, 437 U.S. 267, 272).

As to Commerce Clause challenges, one strand of earlier cases applied a formalistic approach prohibiting the imposition of what the Court deemed a "direct" tax on interstate commerce (*see, Spector Motor Serv., Inc. v O'Connor*, 340 U.S. 602; *Freeman v Hewitt*, 329 U.S. 249). Except for such taxes found to directly burden interstate commerce, the Court recognized that the

Commerce Clause did not "relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business" (*Western Live Stock v Bureau of Revenue*, 303 U.S. 250, 254). Accordingly, other forms of nondiscriminatory taxation on interstate transactions were permitted. A nexus was required, however, between the taxing state and the entity, property or activity it sought to tax.

Little difficulty was encountered in finding the required local nexus with respect to sales and compensating use taxes. In *McGoldrick v Berwind-White Coal Mining Co.* (309 U.S. 33), the vendor's responsibility to collect the tax on the sale of coal by a Pennsylvania producer to a New York City purchaser was upheld because "the tax is conditioned upon a *local activity*, delivery of goods within the state upon their purchase for consumption" (*id.*, at 58 [emphasis supplied]).

Until *Quill Corp. v North Dakota*, the constitutionally required nexus between the taxing State and the activity, entity or property subject to the tax was applied indistinguishably for purposes of both Due Process and Commerce Clause analysis, *i.e.*, a definite link or minimum connection (see, *National Bellas Hess, Inc. v Department of Revenue of Illinois*, 386 U.S. 753, 756-757; *Scripto, Inc. v Carson*, 362 U.S. 207, 210-211). Some physical presence of the vendor in the taxing State was noted as a factor justifying the imposition of the sales and use tax collection obligation. In *Felt & Tarrant Mfg. Co. v Gallagher* (306 U.S. 62) that presence was found in the foreign seller's engagement of two non-employee commissioned sales agents to solicit orders and the rental of office space for them. In *Scripto, Inc. v Carson* (*supra*), ten wholly commissioned non-employee "advertising specialty brokers" (*id.*, at 209), retained on a part-time, nonexclusive basis to solicit sales, constituted a sufficient physical connection.

In *National Bellas Hess, Inc. v Department of Revenue of Illinois* (386 U.S. 753), the Court for the first time explicitly made some physical presence of the vendor in the taxing State a requirement under both the Commerce and Due Process Clauses

for charging the vendor with the duty of collecting a use tax on mail-order purchases by residents of that State. Physical presence within the taxing State was required, irrespective of the degree to which the vendor may have availed itself of the benefits and protection of the taxing State in other ways, such as by "regularly and continuously engaging in 'exploitation of the consumer market' of [that State]" (*id.*, at 762 [Fortas, J., dissenting] [quoting *Miller Bros. Co. v Maryland, supra*]). In *Bellas Hess*, the vendor's patronage in the taxing State was exclusively through mail-order purchases, and its only contact with its customers was by way of the United States mails or by common carrier.

The Court in *Bellas Hess* gave three reasons for requiring the vendor's physical presence in the taxing State: (1) without some physical presence, there would be no fair basis for making interstate commerce bear a share of the cost of local government; (2) a contrary rule would require the Court "to repudiate *totally* the *sharp* distinction", relied upon by State taxing authorities, between mail order sellers with local outlets or solicitors and "those *who do no more* than communicate with customers in the state by mail or common carrier as part of a general interstate business" (386 US, at 758 [emphasis supplied]); and (3) permitting imposition of the duty of collection of the tax in that case would subject national mail order businesses to oppressive administrative and record-keeping burdens "in a virtual welter of complicated obligations to local jurisdictions with no legitimate claim to impose 'a fair share of the cost of the local government'" (*id.*, at 759).

As reflected in the cases following *Bellas Hess*, the requirement of the vendor's physical presence in the taxing State was not unduly exacting. In *Standard Pressed Steel Co. v Washington Dept. of Revenue* (419 U.S. 560), the Court upheld the assessment of a Washington State gross receipts tax on a foreign vendor's sales to the Boeing Company against Due Process and Commerce Clause challenges. The Court found a sufficient vendor's physical presence in the State to justify the tax in the person of a single resident engineer-employee who operated out of his home in Seattle and whose responsibilities were to consult

with Boeing on anticipated needs for the vendor's parts in Boeing's aircraft manufacturing process and to follow up on shipping or other problems in using the vendor's product (*id.*, at 562-563). In *Goldberg v Sweet* (488 U.S. 252), at issue was Illinois' imposition of a five percent excise tax on interstate telephone calls which the taxing statute required to be collected by long-distance telephone carriers, such as GTE Sprint Communications (Sprint), through their billings. Sprint challenged the tax, but it and the other parties did not contest (and the Court agreed) that the local nexus requirement was met because the tax was restricted to telephone calls originating or terminating in Illinois and charged to an Illinois service address (*id.*, at 263). In concluding that a sufficient local nexus existed, the Court did not inquire further into the extent of Sprint's physical presence in the State.

Two other decisions are significant for their articulation of the criteria to determine whether a given tax imposed on interstate commercial activity passes constitutional muster under the Commerce Clause. In *Complete Auto Transit v Brady* (430 U.S. 274), the Court repudiated the artificial and confusing formalistic distinction between direct and indirect taxes on interstate commerce, and overruled *Spector Motor Service v O'Connor* (*supra*) and *Freeman v Hewitt* (*supra*). It explicitly confirmed its agreement with the approach of the alternative line of decisions (some of which we have discussed), such as *Western Live Stock v Bureau of Revenue* (303 U.S. 250, *supra*). The Court characterized those decisions as having "considered * * * the practical effect [of the taxing statute] and sustained * * * the tax * * * when the tax [1] is applied to an activity with a substantial nexus with the taxing state, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State" (430 US, at 279). The Complete Auto articulation of the four-pronged standard for determining the validity of a State tax on interstate commercial activity under the dormant Commerce Clause remains the prevailing test, with refinements, to this day (see, *Oklahoma Tax*

Commn. v Jefferson Lines, Inc., *supra*, 514 US, at ____, 115 S. Ct., at 1337, *supra*).

One such refinement of *Complete Auto* was made at the same term in *National Geographic Socy. v California Bd. of Equalization* (430 U.S. 551). There the Court upheld a use tax collection obligation with respect to interstate mail order sales of the Society from its District of Columbia home office, on the basis of the physical presence of two National Geographic magazine advertising sales offices in the taxing State. The Court made two significant rulings: (1) the required nexus with the taxing state need not necessarily be directly related to the activity being taxed, "but [could] simply [be] whether the facts demonstrate 'some definite link, some minimum connection, between [the taxing State] and the person it seeks to tax'" (*id.*, at 561 [quoting *Miller Brothers v Maryland*, *supra*] [emphasis supplied]); and (2) the required physical presence of the vendor in the taxing State must be more than the "'slightest presence'" (*id.*, at 556).

II.

It is with the foregoing decisional evolution of negative Commerce Clause doctrine by the Supreme Court in mind that we turn to *Quill Corp. v North Dakota* (504 U.S. 298, 112 S Ct 904, *supra*). *Quill Corp.*, like *National Bellas Hess*, involved a vendor exclusively engaged in a mail-order business with substantial patronage in the taxing State, but whose only connection with its customers in that State was by common carrier or the United States mail. The Supreme Court of North Dakota held, nonetheless, that social, technological, economic, commercial and legal changes since *Bellas Hess* was decided rendered the holding in that case obsolete. The North Dakota Court concluded that physical presence was no longer necessary in the case of a mail-order vendor who systematically directed its marketing efforts at the taxing State. The State Supreme Court pointed out that North Dakota had expended significant resources to create and nurture an economic climate supporting a demand for Quill's products, had provided a legal infrastructure that protected and secured Quill's financial interests, and had disposed as waste

many tons of Quill's catalogs and promotional materials mailed to the State. Therefore, the North Dakota Supreme Court reasoned, the Commerce Clause should not bar making Quill pay its fair share for those benefits and protections it received from the State. The United States Supreme Court noted that it was thus confronted with a pull in one direction from the approach emphasized in *Complete Auto Transit* adjudging a State tax for Commerce Clause purposes based upon economic realities and practical effects, and the opposing magnetism of stare decisis. "Having granted certiorari * * * we must either reverse the State Supreme Court or overrule *Bellas Hess*. *While we agree with much of the State court's reasoning*, we take the former course" (504 US, at 301-302 [emphasis supplied]).

In actuality, however, the Supreme Court in *Quill* adopted a middle course. It overruled so much of *Bellas Hess* as required some physical presence of the vendor as a "minimum connection" in the taxing State to support the jurisdiction to tax under the Due Process Clause (504 US, at 306, 307-308).[2] However, the Supreme Court in *Quill* elected to adhere to the *Bellas Hess* precedent requiring some physical presence of an interstate mail-order vendor in the taxing State for validity under the Commerce Clause. This course was not adopted without some apparent reluctance. Thus, the Court stated that, "while contemporary Commerce Clause jurisprudence might not dictate the same result were the issue to arise for the first time today, *Bellas Hess* is not inconsistent with *Complete Auto*" (504 US, at 311). It further stated, "*[a]lthough we agree with the State Court's assessment* of the evolution of our cases, we do not share its conclusion that this evolution indicates that the Commerce Clause ruling of *Bellas Hess* is no longer good law" (504 US, at 314 [emphasis supplied]).

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[2] Because minimum physical presence in the taxing State is no longer required to support jurisdiction to tax under the Due Process Clause, the authority of *Miller Bros. Co. v Maryland* (374 U.S. 340), a pure due process case — heavily relied upon by the dissent — is considerably weakened.

The rationale of the Supreme Court in *Quill* for continuing to require the physical presence of the vendor in the taxing State, however, was not the same primarily relied upon in *Bellas Hess*, that only by requiring a physical presence in the taxing State can the vendor justifiably be called upon to pay its fair share of the cost of local government. The Supreme Court agreed with the North Dakota Supreme Court's conclusion that, under the more "flexible" approach of current Commerce Clause jurisprudence (504 US, at 314), the *quid pro quo* for State taxation could be found in the benefits and protections the State confers in providing for a stable and secure legal economic environment for a mail-order vendor's substantial marketing efforts aimed at the taxing State. Rather, the justification for continuing to require a physical presence of the vendor in the taxing State was based on two other grounds. First, *Bellas Hess* furthers the ends of the Commerce Clause by furnishing a "'bright-line' test[]" (504 US, 314), a "demarcation of a discrete realm of commercial activity that is free from interstate taxation" (*id.*). The *Bellas Hess* rule, thus, serves to assure tax immunity to "vendors 'whose *only connection* with customers in the (taxing] State is by common carrier or the United States mail'" (*id.* [emphasis supplied]). Such a bright-line demarcation benefits national commerce by avoiding the litigation-provoking controversy and confusion of imprecise constitutional standards, and fosters investment by settling expectations (*id.*). Second, adherence to the *Bellas Hess* physical presence requirement satisfies the especially applicable demands of stare decisis. "The *Bellas Hess* rule has engendered substantial reliance and has become part of a basic framework of a sizable industry. The interest in stability and orderly development of the law' that undergirds the doctrine of stare decisis' * * * therefore counsels adherence to settled precedent" (504 US, at 317).

III.

As the foregoing discussion demonstrates, both the literal language of the *Quill* decision and consideration of its place in the evolution of Supreme Court Commerce Clause jurisprudence refute the Appellate Division's conclusion, urged by Orvis and

VIP here, that "*Quill* * * * *increased* the requisite threshold of in-State physical presence from any measurable amount of in-State people or property to *substantial amounts* of in-State people or property" (204 AD2d, at 917 [emphasis supplied]). *Quill* simply cannot be read as equating a substantial physical presence of the vendor in the taxing State with the substantial nexus prong of the *Complete Auto* test, as the Appellate Division's interpretation would require.

First, neither in *Bellas Hess* nor in the cases preceding it, or succeeding it up to *Quill* did the Court express any insistence that the physical presence of the interstate vendor be substantial for a valid taxation of sales of or imposition of a use tax collection duty upon the vendor. *Bellas Hess* itself, in requiring the vendor's physical presence, explicitly stated that it was applying a definite link or minimum connection requirement, which was the then prevailing nexus standard for both Due Process and Commerce Clause analysis in interstate commerce taxation cases (*see*, *supra*, 386 US, at 756-757, *supra*). Surely as a matter of simple logic and semantics, the Supreme Court was not applying a *substantial* physical presence requirement when it upheld the State tax on the in-State activity of the interstate vendor in the following cases: *Felt & Tarrant Mfg. Co. v Gallagher* (306 U.S. 62, *supra*) (two non-employee commissioned sales solicitors); *Scripto, Inc. v Carson* (362 U.S. 207, *supra*) (10 part-time non-employee nonexclusive, commission sales brokers); *Standard Pressed Steel Co. v Washington* (419 U.S. 560, *supra*) (one engineer-consultant operating an office out of his home); *Goldberg v Sweet* (488 U.S. 252, *supra*) (an interstate long-distance telephone carrier's billing to an in-State service address for calls originating or terminating in the taxing State).

As we have shown from the Court's own expressions in *Quill*, rather than expanding upon the *Bellas Hess* minimum connection physical presence requirement, the *Quill* decision cannot be substantively construed as other than a somewhat begrudging retention of the *Bellas Hess* physical presence requirement — a "result", as the Court in its opinion remarked, "not dictated * * *

were the issue to arise for the first time today" (*Quill Corp. v North Dakota, supra*, 504 US, at 311, *supra*).

Even more importantly, acceptance of the thesis urged by Orvis and VIP — that *Quill* made the substantial nexus prong of the *Complete Auto* test an in-State substantial physical presence requirement — would destroy the bright-line rule the Supreme Court in *Quill* thought it was preserving in declining completely to overrule *Bellas Hess*. Inevitably, a *substantial* physical presence test would require a "case-by-case evaluation of the actual burden imposed" (504 US, at 315) on the individual vendor involving a weighing of factors such as number of local visits, size of local sales offices, intensity of direct solicitations, etc., rather than the clear-cut line of demarcation the Supreme Court sought to keep intact by its decision in *Quill*. Thus, ironically, the interpretation of *Quill* urged by the vendors here would undermine the principal justification the Supreme Court advanced for its decision in that case, the need to provide certainty in application of the standard and with it, repose from controversy and litigation for taxing States and the nearly $ 200 billion-a-year mail-order industry, with respect to sales and use taxes on interstate transactions.

Finally, confirmation that the Supreme Court never intended to elevate the nexus requirement to a substantial physical presence of the vendor can be found in *Oklahoma Tax Commn. v Jefferson Lines, Inc.* (514 U.S. _____, 115 S. Ct. 1331, *supra*), the Supreme Court's most recent pronouncement in the interstate sales and use tax field. In that case, the Court did not apply a substantial physical presence test, but instead strictly utilized the substantial nexus prong of the *Complete Auto* test without even passing reference to the substantiality of the physical presence of the vendor (an interstate bus company) in the taxing State. Relying upon landmark cases decided before *Quill*, the Court focused on the in-State activity involved in the taxed transaction, such as the site of the origination or consummation of the transaction the State sought to tax (*see, id.*, 514 US, at 1338 [citing *McGoldrick v Berwind-White Coal Mining Co., supra*, 309 U.S. 33; *Goldberg v Sweet, supra*, 488 U.S. 252]). "Oklahoma

is where the ticket is purchased, and the service originates there. These facts are enough for concluding that 'there is nexus aplenty here'" (*id.*, 514 U.S. at __, 115 S. Ct., at 1338).

We think the foregoing survey of the decisional law discloses the true import of the physical presence requirement within the substantial nexus prong of the *Complete Auto* test under contemporary Commerce Clause analysis. While a physical presence of the vendor is required, it need not be substantial. Rather, it must be demonstrably more than a "slightest presence" (*see, National Geographic Society v California Bd. of Equalization*, 430 U.S. 551, *supra*). And it may be manifested by the presence in the taxing State of the vendor's property or the conduct of economic activities in the taxing State performed by the vendor's personnel or on its behalf.

IV.

Applying the foregoing standard for a vendor's physical presence in the taxing state we think is required under *Quill Corp.* and *Bellas Hess*, we conclude that there was substantial evidence to support the State Tax Appeals Tribunal's determination that the activity of Orvis and of VIP in this State were sufficient to impose the obligation to collect compensating use taxes on their taxable retail sales to New York customers. Neither Orvis nor VIP sustained its definite burden of establishing immunity under the Commerce Clause from that tax collection obligation (*see, General Motors Corp. v Washington*, 377 U.S. 436, 441; *Norton Co. v Dept. of Revenue*, 340 U.S. 534, 537), nor their general burden under our case law of proving sufficient facts to overcome an assessment and to demonstrate that the determination of the State Tax Appeals Tribunal was clearly erroneous (*Matter of Grace v New York State Tax Commission*, 37 NY2d 193, 195-196).

In a March 1981 written response to an inquiry from a State Sales Tax auditor, Orvis' treasurer described its operations in New York as follows: "Some salesmen who reside in Vermont travel into New York to call on non-Orvis owned stores. These salesmen in no way bind the Orvis Co., all orders are approved

in Vermont." A subsequent audit of Orvis' records disclosed that during the three years under audit, Orvis' annual sales to New York customers varied from $ 1 million to $ 1.5 million, about 15% of which consisted of wholesale purchases made by from nine to 16 unaffiliated New York retail establishments. Contrary to the holding of the Appellate Division, the foregoing evidence supported a reasonable inference by the Tax Appeals Tribunal that Orvis' substantial wholesale business in this State was generally accomplished by means of its sales personnel's direct solicitation of retailers through visits to their stores in New York, subject only to approval of all orders in Vermont.[3] This sales activity in New York would presumptively suffice as a nexus to impose a use tax collection responsibility (*see, Felt & Tarrant Mfg. Co. v Gallagher*, 306 U.S. 62, *supra*; *see also, National Geographic Society v California Bd. of Equalization*, 430 U.S. 551 [required vendor's presence need not directly relate to the taxed activity]).

It was not unreasonable for the Tribunal to give little if any weight to the affidavits Orvis submitted of its president and treasurer averring that there were only 12 visits to New York retailers by Orvis personnel during the audit period and not for the purposes of sales promotion but only to discuss problems such as concerning shipping and to check on how Orvis products were displayed. It is true, as noted by the Appellate Division, that the Regulations of the State Department of Taxation and Finance authorize the submission of affidavits in lieu of oral testimony (see, 20 NYCRR 3000.10[d][1]). The existence of the regulation did not, however, prevent the Tribunal from rejecting the

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[3] A form letter Orvis sent to retail establishments showed that Orvis extended credit to wholesale purchasers and that it imposed a "minimum stocking order of $3000" upon its wholesale customers. This evidence supports the conclusions (1) that the wholesale orders from sales solicitations in New York (admitted in Orvis' March 1981 letter) were indeed substantial, and (2) Orvis, in extending credit to New York wholesale purchasers, necessarily relied upon and utilized the banking and legal systems of this State.

credibility of the affidavits submitted under the circumstances presented in this case. The fact is, on the crucial issue in this litigation, Orvis declined to expose its witnesses to cross examination by producing them at the hearing before the State Tax Appeals Tribunal. As the Tribunal also noted in discrediting the affidavits, their description of the purposes of Orvis contacts with retailers in this State was indeed inconsistent with the admissions against Orvis' interest contained in its initial response to the inquiry of New York taxing authorities. The Tribunal, in relying on the foregoing factors did not act artibrary or capriciously in concluding that the Orvis affidavits lacked credibility.

Moreover, the affidavits of Orvis' officers described the trips to New York of Orvis personnel as "in a loop", suggesting systematic visitation to all of its as many as 19 wholesale customers on the average of four times a year. This demonstrably exceeded the "slightest presence" of Orvis in New York (*National Geographic Society v California Bd. of Equalization, supra*). Without even a credible let alone cogent explanation of why the March 1981 portrayal of Orvis' sales activity physically occurring in New York was inaccurate, the State Tax Appeals Tribunal was not arbitrary or capricious in concluding that Orvis failed to meet its burden of demonstrating its constitutional immunity. We have also considered Orvis' additional objections to the assessment and penalties imposed and find them equally unpersuasive. However, additional arguments raised by Orvis to the Appellate Division, and not considered by that Court, need to be remitted to that Court for its disposition. Also before us is Orvis' cross appeal to this Court seeking recovery of attorney's fees. Inasmuch as Orvis has not succeeded on the merits of its constitutional challenge to the tax assessment, it has no entitlement to such fees.

There likewise was substantial evidence to support the Tax Appeal Tribunal's determination upholding the sales and use tax assessment against VIP. Evidence was submitted from which the Tribunal could reasonably infer that VIP's hardware and software sales agreements obligated it to provide a charge-free visit of a

VIP computer software installer at its beverage-distributor customer's site in New York if problems necessitating the visit occurred within the first 60 days of installation. Moreover, VIP's invoices showed charges for travel expenses to its New York customers' locations on 41 occasions, in order to resolve the more intractable problems involving its computer hardware and software, during the three year audit period, in which VIP had 154 taxable transactions in New York. There was ample support in the record for the State Tax Appeals Tribunal's finding that VIP's trouble-shooting visits to New York vendees and its assurances to prospective customers that it would make such visits enhanced sales and significantly contributed to VIP's ability to establish and maintain a market for the computer hardware and software it sold in New York. VIP's activities in New York were, thus, definite and of greater significance than merely a slightest presence (*see, Standard Steel Co. v Washington Revenue Department, supra*, 419 U.S. 560, 562 (in-State presence of a single employee of vendor "made possible the realization and continuance of valuable contractual relations between the (interstate vendor and its customer)"]). As with Orvis, we find VIP's additional objections to the assessment and penalties equally without merit.

Accordingly, the judgment in *Matter of Orvis Company v Tax Appeals Tribunal of State of New York* should be modified in accordance with the opinion herein, and the matter remitted to the Appellate Division for consideration of issues raised but not reached at that Court. The judgment in *Matter of Vermont Information Processing, Inc. v Tax Appeals Tribunal of State of New York* should be reversed, and the determination of respondent Tax Appeals Tribunal reinstated and confirmed and the petition dismissed, with costs.

BELLACOSA, J. (dissenting):

Because we agree with the Appellate Division's grant of the respective petitions to annul the determinations of the Tax Appeals Tribunal, we respectfully dissent and vote to affirm in each case.

The Court is unanimous that the governing constitutional standard is "substantial nexus" of the taxpayer's business activities to the taxing State and not "substantial physical presence." Judge Ciparick and I conclude, however, that the minuscule, infrequent activities in New York by the two Vermont vendors do not satisfy the "substantial nexus" threshold requirement imposed by the Commerce Clause of the United States Constitution (art I, § 8, cl 3), and the governing interpretations promulgated by the United States Supreme Court.

It seems to us that the majority's articulation miscasts the evolution of United States Supreme Court Commerce Clause precedents and injects confusion when a "substantial nexus" bright line has been the guiding hallmark and jurisprudential goal. Functionally and commercially, telling out-of-state businesses that they dare not dip their toes within New York's borders without incurring New York taxes is not the teaching of the United States Supreme Court cases. Rather, deterring interstate traffic in such respects by taxation is precisely what is forbidden under the mantle of the Commerce Clause. Thus, absent evidence of a "small sales force, plant, or office" (*Quill Corp. v North Dakota*, 504 U.S. 298, 315), or "*continuous* local solicitation" (*Scripto, Inc. v Carson*, 362 U.S. 207, 211 [emphasis added]), within New York State, imposition of the taxes at issue should be unconstitutional.

The question devolves to whether Orvis Co., Inc. and Vermont Information Processing, Inc., businesses not authorized and not doing business in New York, nevertheless by their minimal acts or course of business venturings arising out of sporadic commercial transactions in New York, entangled themselves in New York State's wide taxing web.

A State may not tax the economic activity of a foreign business engaged in interstate commerce unless "the tax is applied to an activity with a *substantial nexus* with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State" (*Complete Auto Transit, Inc. v Brady*, 430 U.S. 274, 279 [1977]

[emphasis added]). The Supreme Court has repeatedly applied this principle in subsequent cases, most recently in *Oklahoma Tax Commn. v Jefferson Lines, Inc.*, 514 U.S. __, __, 115 S. Ct 1331, 1338 [April 3, 1995]). The present cases turn solely on the first prong, *i.e.*, whether New York has a substantial nexus with the interstate activities of these two Vermont businesses to sustain a New York State sales and use tax.

A precise appreciation and reflection of the precedential building blocks is essential in this highly technical field. In *National Bellas Hess, Inc. v Dept. of Revenue of Illinois* (386 U.S. 753 [1967]), the State of Illinois sought to impose a use tax on National, a mail order business with its principal place of business in Missouri. National did not own any real property, maintain an office, sales house or warehouse in Illinois, and it did not have any agents, salespeople or other type of continuous representation in Illinois. National's only link to Illinois was via the United States mail or a common carrier.

Under Illinois statute, National was required to collect and pay to the State a tax imposed upon Illinois consumers who purchase the company's goods for use in the State. National argued that the tax created an unconstitutional burden upon interstate commerce. The Supreme Court ruled in favor of the putative taxpayer. The Court declared that "if Illinois can impose such burdens, so can every other State, and so, indeed, can every municipality, every school district, and every other political subdivision throughout the Nation" (*id.*, at 759). In 1992, the Supreme Court ruled in *Quill Corp. v North Dakota* (504 U.S. 298, *supra*) that *Bellas Hess* was still valid, operative and consistent with its decision in *Complete Auto Transit, Inc. v Brady* (430 U.S. 274, *supra*).

Quill settled two important facets of the rules. First, the nexus requirements of the Due Process and Commerce Clauses are not the same. Thus, a foreign corporation may engage in "minimum contacts" to satisfy the Due Process Clause, but still lack "substantial nexus" to support a State's taxing reach under the Commerce Clause. Second, the imposition of the duty to collect

sales and use taxes on a foreign corporation is subject to a physical presence or functional equivalent requirement. The Court stated:

> Like other bright-line tests, the *Bellas Hess* rule appears artificial at its edges: Whether or not a State may compel a vender to collect a sales or use tax may turn on the presence in the taxing State of a small sales force, plant, or office. This artificiality, however, is more than offset by the benefits of a clear rule. Such a rule firmly established the boundaries of legitimate state authority to impose a duty to collect sales and use taxes and reduces litigation concerning those taxes.* * * [A] bright line rule in the area of sales and use taxes also encourages settled expectations and, in doing so, fosters investment by businesses and individuals (citations omitted) (*Quill*, *supra*, at 315-316).

New York's approach, now approved by this Court in the instant two cases, contradicts that rationale, certainty and the bright-line approach. It allows businesses to be tax-nicked at the "edges." Notably, *Quill* excludes from interstate taxation commercial activities which are not based on the physical presence of a "small sales force, plant, or office" in the taxing State (*id.*, at 315). Accordingly, sporadic sojourns into a state will not supply an adequate nexus to overcome the Commerce Clause protection (*compare*, *Miller Bros. Co. v Maryland*, 347 U.S. 340,346-347 [a Due Process Clause case]).

We disagree with the majority's suggestion that *Miller Bros. Co. v Maryland* (*supra*) is essentially irrelevant (Majority opn, at Il, n2). *Miller* required the demonstration of "some definite link, some minimum connection, between a state and the person * * * or transaction it seeks to tax" (347 US, at 344-345), and the Supreme Court ruled not to allow the imposition of the use tax on the Delaware merchandiser (*Miller Bros. Co. v Maryland*, 347 U.S. 340, 340-345, *supra*). The case rests on a different analysis of economic exploitation of consumer markets. Thus, it retains its vitality, relevance and analogous usefulness to the distinct analysis and disposition of the instant case.

The following cases are also important to scan the full landscape. In *National Geographic Socy. v California Bd. of Equalization* (430 U.S. 551 [1977]), the Supreme Court held that the State of California's imposition of a use tax liability on the Society's mail-order operation did not violate the Commerce Clause, since the Society had *two offices* in the State of California and "activities there adequately established a relationship or 'nexus' between the [magazine] and the State" sufficient to support the tax (*id.*, at 556). Similarly, in *Standard Pressed Steel Co. v Department of Revenue of Washington* (419 U.S. 560), the State of Washington's imposition of a tax levied on Standard's unapportioned gross receipts of sales made to Boeing Company, in Seattle, was not repugnant to the Commerce Clause, since one of Standard's employees maintained an office in the State of Washington (*see also, Tyler Pipe Indus. Inc. v Washington State Dept. of Revenue*, 483 U.S. 232; *D.H. Holmes Co., Ltd. v McNamara*, 486 U.S. 24, 32). Furthermore, in *Felt & Tarrant Mfg. Co. v Gallagher* (306 U.S. 62, 64), the State of California sought to impose a use tax against an Illinois corporation. The Court upheld the imposition of the tax where the Illinois corporation had hired two general agents to solicit sales orders in California and contracted to pay the rent of a California *office* maintained for each agent (*see also, Moorman Mfg. Co. v Bair, Director of Revenue of Iowa*, 437 U.S. 267; *General Motors Corp. v Washington*, 377 U.S. 436; *accord, Nelson v Sears, Roebuck & Co.*, 312 U.S. 359; *Nelson v Montgomery Ward & Co., Inc.*, 312 U.S. 373 [no Commerce Clause violation where sellers maintained local retail stores in taxing state]).

Importantly, in the absence of an in-state plant or office, substantial nexus has been found to exist only when the foreign vendor maintains "*continuous local solicitation*" within the taxing State (*Scripto, Inc. v Carson*, 362 U.S. 207, 211, *supra* [emphasis added]; *Miller Bros. Co. v Maryland*, 347 U.S. 340, 346, *supra*; *see, National Geographic Socy. v California Bd. of Equalization*, 430 U.S. 551,557, *supra*; *National Bellas Hess, Inc. v Dept. of Revenue of Illinois*, 386 U.S. 753,757, *supra*). In *Scripto*, a Georgia corporation sold certain mechanical writing

instruments to Florida residents. Scripto did not own or lease any office or plant in Florida. However, the corporation had written contracts with 10 sales "brokers," who were residents of Florida. The detailed contracts described the brokers as representatives of "Scripto for the purpose of attracting, soliciting and obtaining Florida customers." Although the salespeople were independent contractors, they provided Scripto with "continuous local solicitations in Florida," which satisfied the substantial nexus requirement (*Scripto, Inc. v Carson*, 362 U.S. 207,211, *supra*).

The instant cases fall neither under *Scripto* nor *National Geographic*. The majority, we respectfully suggest, focuses too narrowly on the legal relationship between Scripto and its agents, rather than on the regularity and durational aspects of the agents' economic activities in the taxing State. The latter features are dispositive and key under the legal tests in *Quill* and *Scripto*. The Supreme Court expressly stated that the fact that "the salespeople were not regular employees of [Scripto] devoting full time to its service" had no constitutional significance, because "the test is simply the *nature and extent of the activities* * * * in [the taxing State]" (*Scripto, Inc. v Carson*, *supra*, at 211-212 [emphasis added]). Highly significantly in these cases involving our application of exclusively governing Supreme Court jurisprudence is the fact that the Supreme Court itself has repeatedly stated that *Scripto, Inc. v Carson* (*supra*) "represents the furthest constitutional reach to date of a State's powers to deputize an out-of-state retailer as its collection agent for a use tax" (*National Bellas Hess, Inc. v Dept. of Revenue of Illinois*, 386 U.S. 753, 757, *supra*; *see*, *Quill Corp. v North Dakota*, 504 U.S. 298, 306, *supra*). We believe that the instant cases go "further".

Relevantly, in *General Trading Co. v State Tax Commissioner* (322 U.S. 335), a Minnesota corporation, which maintained no office or place of business in Iowa, solicited sales in Iowa by salespeople from head-quarters in Minnesota where the goods were shipped by common carrier into Iowa. The United States Supreme Court made no mention in the decision of the number of salespeople or the regularity of their excursions to solicit sales in Iowa. However, in referencing the facts of *General Trading* in

a Due Process Clause case, *Miller Bros. Co. v Maryland* (347 U.S. 340, 346, *supra*), the Supreme Court noted "that was the case of an out-of-state merchant entering the taxing state through traveling sales agents to conduct *continuous local solicitation* * * * the only nonlocal phase of the total sale being acceptance of the order" (emphasis added). Indeed, it was the absence of continuous local solicitation which led the Supreme Court in *Miller Bros.* (*supra*) to hold that the State of Maryland could not impose the duty to collect a use tax on a Delaware merchandising corporation, although Miller made occasional deliveries into Maryland.

These precedents, taken together, in our respectfully tendered view, provide no constitutional hook to sustain the imposition of sales and use taxes assessed against these two Vermont vendors. The Tax Appeals Tribunal acknowledged that neither vendor maintained, leased or owned any office, distribution house or any other place of business in New York; nor do they own any tangible property, real or personal in New York; nor do they have a telephone listing in New York; nor do they have any agents or representatives stationed in New York. They, thus, have not provided New York with the key to the tax coffers box — a *substantial* nexus to New York by their activities here.

Orvis Co., Inc. submitted two affidavits to rebut the imposition of the use tax. The first affidavit, dated November 16, 1990, was signed by Leigh H. Perkins, president of the Orvis Company, Inc. Perkins stated that employees of Orvis' wholesale division visited New York retailers on a "sporadic, irregular basis." The purpose of the visits was to communicate with the retailers about problems in shipments, questions regarding display of the product, and to inspect the establishments of retailers selling Orvis products. Lastly, Perkins stated that "the purpose of these visits was not to solicit sales to retailers nor to obtain purchase orders from the retailers."

The second affidavit, dated November 19, 1990, was signed by Thomas S. Vaccaro, a vice president and the treasurer of the Orvis Company, Inc. Vaccaro's affidavit repeated many of the

same facts set forth in Perkins' affidavit, but also attached a worksheet depicting the number of trips in New York State taken by Orvis Co., Inc. wholesale division employees during the assessment period, September 1, 1977 through August 31, 1980. During the 36-month assessment period, Orvis' employees made 12 trips to New York. The State relies on a letter signed by Vaccaro, dated March 27, 1981. In that letter, Vaccaro stated that "some salesmen who reside in Vermont travel into New York to call on non-Orvis owned stores. The salesmen in no way bind the Orvis Company; all orders are approved in Vermont."

The letter and affidavits honestly acknowledge Orvis' *de minimis*, fleeting dashes into New York State. This is not the stuff of a cognizable, constitutional threshold called "*substantial* nexus," absent any of the other physical presence features of "continuous local solicitation" (*Scripto, Inc. v Carson*, 362 U.S. 207, 211, *supra* [emphasis added]; *Miller Bros. Co. v Maryland*, 347 U.S. 340, 346, *supra*). Orvis' New York drop-ins look very much like Miller's occasional deliveries into Maryland (*see, id.*), and amounted to nothing more than a "*slight*[] presence" in New York (*National Geographic Socy. v California Bd. of Equalization*, 430 U.S. 551,556, *supra* [emphasis added]).

Likewise, Vermont Information Processing, Inc. had no employees in New York, did not employ sales-people to travel into New York to solicit sales, nor did it advertise in New York or engage in direct mail solicitation. Most of VIP's customers heard about VIP's products through word-of-mouth, and it was VIP's policy to invite interested parties to Vermont for demonstrations. If a customer decided to purchase VIP's services, VIP would send a contract by United Parcel Service. The final product, whether it was an entire computer hardware system or simply computer software, was shipped to the customer via common carrier. VIP's customers were usually trained to use the programs developed for them at VIP's headquarters in Vermont. VIP's personnel were available to customers by telephone to resolve problems. In addition, if software modifications were required, VIP installers were able directly to access a customer's computer from VIP's own computer system

in Vermont through the use of a modem. In fact, during the entire assessment period, December 1, 1983 through November 30, 1986, VIP personnel made at most 41 visits to New York to service existing clients, never to solicit new customers. In our view, VIP's relatively occasional sojourns into New York State cannot represent anything more than a slight physical presence, and surely do not qualify as "continuous local solicitation." VIP, like Orvis, lacked continuous presence in New York, which is the *sine qua non* of the "substantial nexus" test.

These businesses evidently tried to conform their business practices to legitimately avoid incurring multistate taxation in accordance with the teaching of *Quill* (*Quill Corp. v North Dakota*, 504 U.S. 298,309-317, *supra*). Despite their best efforts, they are now snagged by the ever-widening net that unsettles expectations, discourages investment and legitimate interstate commercial intercourse and tears at the mantle of Commerce Clause protection.

In sum, the "nature and extent of the activities" (*Scripto, Inc. v Carson*, 362 U.S. 207, 211, *supra*) of these two Vermont vendors are less "substantial" than all previous cases where "substantial nexus" has been found to exist. If the minimal forays in these cases are sufficient for New York to tax these businesses, so, too, can every other state, municipality and political subdivision throughout the nation for minimally qualifying conduct (*National Bellas Hess, Inc. v Dept. of Revenue of Illinois*, 386 U.S. 753, 759, *supra*). Finally and intuitively, these cases present an interesting contradiction in the facts of their minimal conduct and the law of substantial nexus.

No. 138: Judgment modified, with costs to appellant-respondent Commissioner, and matter remitted to the Appellate Division, Third Department, for further proceedings in accordance with the opinion herein and, as so modified, affirmed. Opinion by Judge Levine. Chief Judge Kaye and Judges Simons, Titone and Smith concur. Judge Bellacosa dissents and votes to affirm in a writing in which Judge Ciparick concurs.

No. 139: Judgment reversed, with costs, and petition dismissed. Opinion by Judge Levine. Chief Judge Kaye and Judges Simons, Titone and Smith concur. Judge Bellacosa dissents and votes to affirm in an opinion in which Judge Ciparick concurs.

June 14, 1995, Decided

SUPREME COURT, APPELLATE DIVISION, THIRD DEPARTMENT.

In the Matter of

VERMONT INFORMATION PROCESSING INC.,

Petitioner,

v.

TAX APPEALS TRIBUNAL OF THE STATE OF NEW YORK et al.,

Respondents.

July 28, 1994.

Before MIKOLL, J.P., and MERCURE, WHITE, CASEY and YESAWICH, JJ.

YESAWICH, Justice.

Proceeding pursuant to CPLR article 78 (initiated in this court pursuant to Tax Law § 2016) to review a determination of respondent Tax Appeals Tribunal which sustained a sales and use tax assessment imposed under Tax Law articles 28 and 29.

Petitioner, a Vermont-based corporation, markets computer software and hardware to beverage distributors across the nation. While auditing the records of one of petitioner's New York Customers, the Audit Division of the Department of Taxation and Finance (hereinafter the Division) discovered a letter from petitioner that appeared to refer to activities, carried on by petitioner within this State, that the Division believed to be subject to sales or use tax. Petitioner refused to make its records available for an audit, but an examination of Federal and Vermont tax information led the Division to conclude that petitioner owed sales and use taxes in the amount of $513,112.11, plus penalties and interest, for the period spanning from December 1, 1983 to November 30, 1986.

In its petition seeking administrative review and revision of the assessment — which following a conciliation conference was reduced to $85,172.08 (again, exclusive of penalties and interest) — petitioner asserted that it was not a vendor, as that term is defined by the Tax Law, and was therefore not required to collect and remit sales and use taxes for any of its activities in New York. After an evidentiary hearing, the Administrative Law Judge (hereinafter the ALJ) upheld the assessment, which prior to the hearing had been further reduced to $73,275.04. Respondent Tax Appeals Tribunal upheld the ALJ's determination, finding that petitioner's distribution of brochures to prospective customers in New York satisfied the definition of a "vendor" found in Tax Law former § 1101(b)(8)(i) (in effect during the audit period), as it constituted the solicitation of business within the State, and that site visits made by petitioner's employees to customers in New York, primarily for the purpose of troubleshooting and occasionally installing software, constituted a sufficient nexus with the State to satisfy the constitutional requirements for imposing a duty to collect and remit State use taxes (*see, e.g., National Geographic Socy. v. California Bd. of Equalization*, 430 U.S. 551, 555-556, 97 S.Ct. 1386, 1389-1390, 51 L.Ed.2d 631). Petitioner thereafter commenced this proceeding, in which it seeks to have the decision of the Tribunal set aside as erroneous, illegal and unconstitutional (*see*, Tax Law § 2016).

While petitioner's activities within the State, which include the distribution of brochures to potential customers at their request, satisfy the definition of a "vendor" set forth in the Tax Law and applicable regulations (*see*, Tax Law former § 1101[b][8][i][C]; 20 NYCRR former 526.10[d]), petitioner's contention that it does not have sufficient contacts with New York to satisfy the constitutional prerequisites for imposing a duty to collect and remit use taxes is persuasive. It is settled that the Commerce Clause prohibits the imposition of such a duty upon a party having no "physical presence" in the taxing state (*Quill Corp. v. North Dakota*, ____ U.S. ____, ____ - ____, 112 S.Ct. 1904, 1912-1913, 119 L.Ed.2d 91), and although the U.S. Supreme Court did not indicate in *Quill Corp. v. North Dakota, supra*

exactly how much contact with a state is enough to satisfy the constitutional mandate, it is clear that more than a "slight" presence is necessary (*see, id.* at ____ n. 8, 112 S.Ct. at 1914 n. 8; *Matter of Orvis Co. v. Tax Appeals Tribunal*,___ A.D.2d ___, 612 N.Y.S.2d 503). Thus, if the only contact with customers in the taxing state is by mail or common carrier, or if the only physical presence within the state is an occasional visit by one or more employees, taxation is not permitted (*see, Quill v. North Dakota, supra*, ____ U.S. at ____, 112 S.Ct. at 1914; *Matter of Orvis Co. v. Tax Appeals Tribunal, supra*; *cf., Miller Bros. Co. v. Maryland*, 347 U.S. 340, 74 S.Ct. 535, 98 L.Ed. 744). On the other hand, if employees, agents or independent contractors are permanently stationed in the taxing state for the purpose of soliciting business or performing maintenance or repair, taxation is not proscribed (*see, Scripto, Inc. v. Carson*, 362 U.S. 207, 11, 80 S.Ct. 619, 621, 4 L.Ed.2d 660; *Felt & Tarrant Mfg. Co. v. Gallagher*, 306 U.S. 62, 64-66, 59 S.Ct. 376, 377-378, 83 L.Ed. 488). Here, it is undisputed that petitioner has no office or other place of business, no telephone number, no employees or salespeople, and no means of delivering its products in New York, nor does it advertise in New York newspapers or periodicals. Petitioner's president testified that it is not petitioner's ordinary practice to travel to its customers' places of business, and that on-site visits are only made to approximately 5% of petitioner's customers for the purpose of correcting persistent or difficult problems, or occasionally to install software or train employees. Moreover, the Division auditor's work papers, received in evidence at the hearing, when considered in light of the uncontradicted testimony of petitioner's president, who explained that petitioner does not actually perform any of the hardware installation and maintenance listed on its invoices, indicate no more than 30 or 40 of these visits to New York over a three-year period. This activity, without more, does not rise to the level necessary to justify taxation, for these visits, although perhaps slightly more frequent, are of the same character as those which were found in *Matter of Orvis Co. v. Tax Appeals Tribunal*, ____ A.D.2d ____, 612 N.Y.S.2d 503, *supra* to be inadequate to meet the "nexus" requirement established in *Quill*.

Inasmuch as petitioner has adequately demonstrated that it has no substantial "physical presence" within New York, the Division may not impose upon it a duty to collect and remit a compensating use tax for the tangible personal property it sells here (*see, Matter of Orvis Co. v. Tax Appeals Tribunal, supra*). Consequently, the determination at issue must be annulled.

ADJUDGED that the determination is annulled, with costs, and petition granted.

MIKOLL, J.P., and MERCURE, WHITE and CASEY, JJ., concur.

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition
of
VERMONT INFORMATION
PROCESSING, INC.

DECISION
DTA No. 806207

for Revision of a Determination or for
Refund of Sales and Use Taxes under Articles
28 and 29 of the Tax Law for the Period
December 1, 1983 through November 30, 1986.

Petitioner Vermont Information Processing, Inc., P.O. Box 470, Hercules Drive, Colchester, Vermont 05446 filed an exception to the determination of the Administrative Law Judge issued on February 27, 1992 with respect to its petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1983 through November 30, 1986. Petitioner appeared by James H. Tully, Jr., Esq. The Division of Taxation appeared by William F. Collins, Esq. (Gary Palmer, Esq., of counsel).

Petitioner and the Division of Taxation each filed a memorandum of law. Oral argument, at the request of petitioner, was heard on July 23, 1992.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUES

I. Whether petitioner was a vendor as defined by Tax Law § 1101(b)(8) and thereby required to collect the taxes imposed under Article 28 of the Tax Law.

II. Whether, if petitioner was a vendor pursuant to the Tax Law, the Commerce Clause of the United States Constitution prevents New York from requiring petitioner to collect the use tax imposed by Tax Law § 1110.

III. Whether petitioner has established reasonable cause for its failure to collect and remit the use tax.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge and make additional findings of fact. The Administrative Law Judge's findings of fact and the additional findings of fact are set forth below.

On November 27, 1987, the Division of Taxation ("Division") issued to petitioner, Vermont Information Processing, Inc. ("VIP"), a Notice of Determination and Demand for Payment of Sales and Use Taxes Due for the period December 1, 1983 through November 30, 1986, assessing tax of $513,112.11 plus penalty and interest.

VIP is a Vermont corporation which produces and sells computer software to beverage distributors throughout the United States. During an audit of a beverage distributor located in Troy, New York, an auditor discovered a letter on VIP letterhead which indicated that VIP was making sales in New York State. As a result, the Division commenced an audit of VIP.

VIP was not registered to collect sales and use taxes on behalf of New York State. At the time of the audit, VIP contended that it was not required to register and had no duty to collect New York taxes. On that basis, it refused the Division access to its records. The Division obtained copies of VIP's Federal and Vermont income tax returns and used information from those returns to estimate New York taxable sales for the audit period of $7,330,173.00, with a use tax due on that amount of $513,112.11.

Following a conciliation conference, VIP agreed to allow the auditors to examine its records for the period December 1, 1983

through November 30, 1986. The VIP sales invoices inspected by the Division showed charges for computer hardware, charges for maintenance and installation of that hardware, charges for "site days" (days spent on the customer's business premises), travel expenses, charges for software systems and charges for the installation and maintenance of the software. The Division determined that receipts from the sale and maintenance of the software were not subject to sales or use tax. Charges associated with the sale, maintenance and installation of computer hardware were deemed to be subject to tax. Reimbursements for travel expenses incurred by VIP in connection with service provided to New York customers and charges for site days (days spent at the customer's location) were not deemed taxable by New York. The Division's review of the invoices resulted in a determination of taxable sales of $1,216,744.00. In accordance with this determination, the Division issued a conciliation order, dated September 30, 1988, reducing the tax due to $85,172.08 and sustaining the imposition of penalty. Before hearing, the Division agreed to reduce the amount of tax asserted to $73,275.04.

It is VIP's position that it had no duty to collect and remit New York State sales or use tax, and it challenges the assessment on that basis alone. It concedes that if it is finally determined that VIP was under a duty to collect the tax the amount of tax due for the audit period is $73,275.04.

VIP operates its business from its headquarters in Colchester, Vermont. It does not maintain a place of business in New York. During the audit period, it employed between 20 to 30 workers. Two or three employees were engaged in accounting and bookkeeping operations. Harold Aiken, the president of VIP, and another employee were involved in sales. Approximately four employees were identified as installers. Workers in these positions gathered information from customers regarding the customer's computer system, recordkeeping and business operations. The installers (essentially computer programmers) then adapted VIP computer software to the needs of the customer. The installers also were involved in training the customers to operate the VIP programs. VIP also employed two trainers and

approximately four people to answer questions from customers by telephone.

VIP had no employees in New York and did not employ salesmen to travel into New York to solicit sales, nor did it advertise in New York newspapers or periodicals or engage in direct mail solicitation. Most of its potential customers heard about VIP through word of mouth and contacted VIP to learn more about its product. VIP representatives spoke to potential customers over the telephone and mailed them brochures describing VIP's products and services. Interested parties were invited to Vermont for a demonstration or encouraged to view an operating VIP system at the workplace of an existing VIP customer in New York.

If a beverage distributor decided to purchase VIP's services, the distributor was sent a contract by United Parcel Service ("UPS"). After execution of the contract, the customer was asked to complete a variety of forms which provided VIP with information regarding the customer's business operations and recordkeeping systems. The information supplied by the customer was used by VIP to create software suitable for that customer's particular business operations.

If a customer already possessed a viable computer system, VIP sold only the software programs and VIP's services. If a customer did not already own a computer, VIP would attempt to sell it computer hardware as well. VIP was an industry marketer, authorized by IBM to sell IBM computers to beverage distributors. Mr. Aiken described VIP's relationship with IBM as follows:

> Mr. Aiken: "They [IBM] ship equipment to me, they allow me to have 10 or 15 days credit on the equipment, and then I resell it, but I can only resell it to beverage distributors. They do all installation shippings as if it were sold by their regular representative who might be in Los Angeles. They maintain it by their own maintenance people, and the only thing I'm really doing is adding value to it, and I'm putting my software on it, setting the customer on it, training them, providing him on a

hotline service afterward and an ongoing thing for years and years."

Administrative law judge: "Does your customer have any separate contract with IBM for maintenance, for guarantees or warranties?"

Mr. Aiken: "He would have. The agreement we would have him sign is an IBM agreement, it is not a VIP agreement.... We submit the paperwork so it doesn't get lost or messed up, and he is covered under maintenance by IBM."

Administrative law judge: "And would you separately charge on your invoice for any of that?"

Mr. Aiken: "No." (Hearing Tr., pp. 76-77.)

VIP also sold computer hardware manufactured by a company named MSI and a third company. Its relationship with those companies was similar to its relationship with IBM.

If a VIP transaction included the purchase of computer hardware, the computer was mailed directly to VIP where the software was loaded, and the computer was then shipped by VIP to the customer, via common carrier. If the customer purchased only software, the program was placed on a disk which was shipped to the customer via common carrier.

We make the following additional finding of fact:

Petitioner's president testified that petitioner purchased the computer hardware from the computer manufacturers (IBM, MSI, or the third company) and resold it to petitioner's customers at prices established by petitioner. Petitioner also billed its customers for the installation and initial maintenance of the hardware. Petitioner also sold the computer manufacturer's noncustomized software which petitioner installed on the computer prior to shipping the computer to the customer.

VIP's customers were usually trained to use the programs developed for them at VIP's headquarters in Vermont. As part

of its services, VIP personnel were available to VIP customers by telephone to answer questions and resolve any problems the customer might be having with the VIP computer program. In addition, VIP installers were able to directly access a customer's computer from VIP's own computer system in Vermont through the use of a modem. A customer's computer program could be modified or corrected in this fashion, without the VIP employee leaving Vermont.

VIP personnel did not routinely travel to their customers' locales to answer questions or service customer needs. In fact, it was VIP's policy to discourage travel as much as possible. However, VIP did travel to the customer's place of business if absolutely necessary to install or maintain software or handle problems the customer was having with the software. Mr. Aiken estimated that approximately five percent of its customer accounts required some travel.

We make the following additional finding of fact:

In a small percentage of cases, petitioner's employees visited New York State to hold training sessions for customers on the use of the software programs.

VIP sold its customers on-going services, such as updating the computer programs, for which it charged a monthly fee. VIP used the terms "maintenance" and "installation" to refer to services connected with the software programs; however, VIP did not install or maintain computer hardware or send its employees to its customer's facilities for the purpose of maintaining or installing such hardware. As Mr. Aiken stated in his testimony: "When we call it installation time, that's like you and I talking, it is hours, it is not — I don't have a guy that uses a screwdriver. I don't have that" (Hearing Tr., p. 64). Any computer hardware sold by VIP was installed, serviced and maintained at the customer's business location by employees of the hardware manufacturer.

During the course of the audit, the Division obtained a variety of information which led it to believe that VIP was entering New

York to install both hardware and software at its customers' business locations and that VIP entered New York to conduct training sessions. That information consisted of a letter on VIP letterhead, VIP sales invoices, and conversations with VIP customers. Since VIP vigorously disputes the meaning and importance attributed by the Division to this information, it is necessary to review it in some detail.

(a) The Division introduced a letter dated February 13, 1985 from VIP to a Troy, New York customer. As material here, the letter summarizes computer hardware and software purchased by the customer and contains the following statements:

"PAYMENT SCHEDULE:

Due with this letter (hardware deposit 10%) (received)	3,447.90
Due at installation (hardware 90% + software)	36,481.00

You should budget one to two days at $60.00 per hour for training and installation on the computer and software, as well as actual per diem expenses. Any applicable sales, use, or excise taxes are your responsibility and should be paid to the proper authorities. All VIP charges will be billed when performed.

If John J. Bolond Dist. and VIP determine that an installer is needed on-site for additional data prep within 60 days of installation, VIP will provide that person at no charge to John J. Boland Dist."

The letter also states separate charges for the maintenance of the hardware and software.

An auditor spoke with a representative of the Troy beverage distributor. When asked the substance of that conversation the auditor stated: "They said that the representative installed the computer and trained them and that they had a seminar in Albany in March of 1987." (Hearing Tr., p. 33.)

The auditor believed that the letter provided evidence that VIP entered New York for installation and maintenance of computer hardware and training.

(b) The second document relied on by the Division was a VIP sales invoice to a customer in Athens, New York. The customer was charged for VIP travel time and expenses and for training. The invoice does not indicate where the training took place.

(c) Two other invoices to separate New York customers show charges for software, hardware, hardware maintenance, and "PC/Set Up/Test."[1]

(d) Three invoices to a Plattsburgh customer show miscellaneous travel and transportation expenses and charges for "installation." An auditor spoke with an employee of the Plattsburgh customer and was told that a VIP employee went to the business offices in Plattsburgh to "install system and train him" in its use (Exhibit "M," notation made by auditor).

(e) An invoice to an Ithaca, New York company shows the sale of hardware and software by VIP.

When reviewing the VIP invoices, the auditor made a listing of each invoice which she believed demonstrated VIP's presence in New York in connection with its sales of computer hardware and software in New York. The listing provides the following information for each such invoice: the customer name, the invoice date, the invoice number, the total invoice amount, the amount taxable by New York State, and comments. The comments section identifies those items on the invoice which the auditor construed as evidencing VIP's presence in New York. These items can be separated into two general categories: (1) items of travel expense or charges for site visits and (2) items connected with the installation or maintenance of either computer hardware or software. Approximately 41 invoices contain items

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[1] In his testimony, Mr. Aiken explained this as a charge "to set up a diskette" (Hearing Tr., p. 59).

in the first category. The remaining 40 invoices show charges for items related to installation and maintenance of computer hardware or software. There is no correlation between the hardware installation charges and the travel or site visit charges. For example, invoice number 121188 showed a $480.00 charge for installation of hardware. The auditor included the invoice in the listing of invoices showing a New York presence, presumably because she believed that a VIP employee traveled into New York to install the hardware. The comments section does not indicate that there was a charge for travel expenses, and there is not a separate invoice for travel expenses which can be correlated to the installation found on invoice number 121188. There are some instances where a charge for installation of software is found on the same invoice as a travel expense charge. Invoice number 730 showed an invoice amount of $149.01 for transportation, room, meals and PC installation. None of this was deemed taxable. The invoices do not undermine the credibility of Mr. Aiken's testimony that VIP did not travel to New York to install, service or maintain computer hardware.

After receiving access to VIP's records, the auditor listed all invoices showing sales of property or services subject to sales or use taxes. Her worksheets list approximately 154 such invoices for the audit period.

Mr. Aiken attended a seminar in New York. The subject of the seminar was New York's bottle bill. Mr. Aiken participated as a presenter at the invitation of the seminar's sponsors. The seminar was not conducted for the purpose of training VIP customers or to solicit business in New York, and it occurred after the expiration of the audit period.

VIP registered to do business in New York with the Department of State over 10 years ago. On advice from an attorney, VIP ended its registration. VIP also consulted an accountant about 10 years ago who advised VIP that it had no duty to register as a vendor in New York State or to collect New State use tax.

OPINION

In the determination below, the Administrative Law Judge concluded that: (1) petitioner was a vendor required to collect the use tax on its sales of computer hardware because it solicited business in the State, and by reason of such solicitation made sales of tangible personal property; (2) petitioner failed to meet its burden to show that it did not sell tangible personal property or perform services in New York State taxable under Article 28; (3) petitioner's presence in New York through employee business trips in combination with its other business activity in New York created a sufficient nexus between New York and petitioner to subject petitioner to the obligation to collect use tax; and (4) petitioner did not meet its burden of establishing that its failure to file sales and use tax returns for the period under audit was due to reasonable cause.

On exception, petitioner asserts that: (1) petitioner was not a vendor required to collect sales and use taxes because it did not solicit business in New York; (2) petitioner lacked sufficient nexus with New York State to require it to collect use taxes for its sales in the State as petitioner's activities in the State related solely to the sale of non-taxable products and services; and (3) no penalties should be imposed for petitioner's failure to file sales and use tax returns or to pay taxes due because petitioner relied on Technical Services Bulletin, 1978-1(S), which exempts sellers of customized software from the obligation to collect sales tax on their sales to New York customers, and because petitioner relied on the advice of a third-party accountant.

In response to petitioner's exception, the Division asserts that petitioner's sales in New York of tangible personal property taken together with petitioner's New York presence in connection with its non-taxable sales of intangible personal property and non-taxable services created sufficient nexus under the Due Process and Commerce Clauses of the United States Constitution to require petitioner to collect use tax on its sales of computer hardware to customers in New York.

We affirm the determination of the Administrative Law Judge for the reasons set forth below.

Tax Law § 1110 imposes upon all persons a compensating use tax for use within New York State of any tangible personal property purchased at retail, except to the except that such property has already been subject to sales tax. The obligation to collect the use tax is imposed upon every vendor of tangible personal property (Tax Law §§ 1131[1] and 1132[a]).

In determining whether petitioner was required to collect the taxes imposed under Tax Law § 1110, we must first determine whether petitioner was a vendor as defined by Tax Law § 1101. If it is determined that petitioner was such a vendor, we must then determine whether, under the Commerce Clause of the United States Constitution (US Const art I), sufficient nexus exists between New York and petitioner to allow the imposition of the use tax collection obligation.

Former Tax Law § 1101(b)(8)(i), which was in effect during the audit period,[2] defined a vendor as including:

"(A) A person making sales of tangible personal property or services, the receipts from which are taxed by [Article 28];

(B) A person maintaining a place of business in the state and making sales, whether at such place of business or elsewhere,

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[2] Effective September 1, 1989, the statutory definition of vendor was modified. Tax Law § 1101(b)(8)(i)(C) now defines a vendor, in pertinent part, as:

"A person who solicits business . . .

* * *

(II) by distribution of catalogs or other advertising matter, without regard to whether such distribution is the result of regular or systematic solicitation, if such person has some additional connection with the state which satisfies the nexus requirement of the United States constitution; and by reason thereof makes sales to persons within the state of tangible personal property or services, the use of which is taxed by this article."

to persons within the state of tangible personal property or services, the use of which is taxed by [Article 28];

(C) A person who solicits business either by employees, independent contractors, agents or other representatives or by distribution of catalogs or other advertising matter and by reason thereof makes sales to persons within the state of tangible personal property or services, the use of which is taxed by this article. . . ."

During the audit period, the Division's regulations defining a vendor, in the case of interstate vendors, provided in pertinent part:

"(e) Interstate vendors. (1) A person outside of this State making sales to persons within the State, *who solicits the sales in New York, as defined in subdivision (d) of this section*, of who maintains a place of business as defined in subdivision (c) of this section, is required to collect the sales tax on the tangible personal property delivered in New York or the services performed in New York.

"(2) A person making sales to his customers within the State, who has solicited such sales by the interstate distribution of catalogs or other advertising material by mail and who delivers the merchandise through the mail or by common carrier, and who neither maintains a place of business as defined in subdivision (c) of this section, *nor solicits business as defined in subdivision (d) of this section*, is not required to register as a vendor. However if such person registers voluntarily, he is under the same obligations as any other vendor.

* * *

"Example 3: A person makes sales entirely by catalog in this State from a point outside the State. In addition, he periodically sends repairmen, consultants and others, to maintain the merchandise he sold. He is required to register as a vendor" (former 20 NYCRR 526.10[e], emphasis added).

Soliciting business was defined in former 20 NYCRR 526.10(d) as follows:

"(d) Soliciting business. (1) A person is deemed to be soliciting business if he has employees, salesmen, independent contractors, promotion men, missionary men, service representatives or agents soliciting potential customers in the State.

"(2) A person is deemed to be soliciting business in New York if he distributes catalogs or other advertising material, in any manner in the State."

We conclude that under former Tax Law § 1101(b)(8)(i)(C) petitioner was a vendor obligated to collect the use tax imposed by Tax Law § 1131(1) on every vendor of tangible personal property. Former Tax Law § 1101(b)(8)(i)(C) requires that to be considered a vendor in New York State a person must solicit business within the State and, as a result of such solicitation, make sales to persons within the State of tangible personal property (*see also*, former 20 NYCRR 526.10[e][1]). Petitioner did both and was, therefore, a vendor required to collect the use tax on items taxed by Article 28.

Petitioner's mailing of brochures and other advertising materials to potential customers in New York State meets the definition of soliciting business under Tax Law § 1101(b)(8)(i)(C) and former sales tax regulation 20 NYCRR 526.10(d)(2). Petitioner asserts that its activities did not constitute "solicitation" of business in the State because its brochures were mailed into the State only in response to specific requests for information. In petitioner's view, these mailings should not be considered "solicitation." We disagree. Former Tax Law § 1101(b)(8)(i)(C) does not distinguish between proactive or reactive solicitation.[3] Further,

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[3] The statute states that solicitation includes the "distribution of catalogs or other advertising matter" (former Tax Law § 1101[b][8][i][C]). In addition, former sales tax regulation 20 NYCRR 526.10(d)(2) states that solicitation includes the distribution of advertising materials "*in any*

we cannot see how this would be a meaningful distinction. Regardless of how the potential customers were identified, the purpose of petitioner's mailings was clearly to obtain new customers in the State. It is, therefore, our conclusion that petitioner was soliciting business as defined by the Tax Law.

The case cited by petitioner does not support its view that petitioner's activities did not constitute "solicitation." Petitioner cites *Matter of Koffler v. Joint Bar Assoc.* (51 NY2d 140, 432 NYS2d 872, *cert denied*, 450 US 1026) to demonstrate that its activities do not constitute solicitation (Petitioner's memorandum of law, p. 6). In this case, the Court of Appeals defined "solicit" to mean "to move to action, to endeavor to obtain by asking, and implies personal petition to a particular individual to do a particular thing" (*Matter of Koffler v. Joint Bar Assoc.*, *supra*, 432 NYS2d 872, 875, *citing Webster's Third New Intl. Dictionary* 2169 and *Black's Law Dictionary* 1248-1249 [5th Ed]). The Court in the same opinion contrasted this definition of "solicitation" with that for "advertising," which it defined as "the calling of information to the attention of the public by whatever means" (*Matter of Koffler v. Joint Bar Assoc.*, *supra*, 432 NYS2d 872, 875, *citing*, *Webster's Third New Intl. Dictionary* 31 and *Black's Law Dictionary* 50 [5th Ed.]). Petitioner has repeatedly stated that it did not advertise. However, petitioner's activities fall directly within the Court's definition of "solicitation." Petitioner's directed mailings to potential customers were certainly intended to move particular New York entities to become VIP's customers. Thus, this case further supports our determination that petitioner's activities constituted "solicitation."

The Administrative Law Judge concluded that, as a result of petitioner's solicitation activities within New York, petitioner made sales of tangible personal property consisting of the computer hardware. We agree. Petitioner asserts, however, that even if it was engaged in solicitation activities, it did not make sales in New York of tangible personal property but, rather, its

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manner."

sales were limited to sales of customized computer software and the maintenance thereof, both non-taxable activities under the Tax Law. Petitioner's claim appears to be that petitioner did not sell the computer hardware, but rather, the computer hardware was purchased by petitioner's customers from the computer manufacturer. The record below does not support this conclusion. Petitioner solicited the sales of computer hardware from its potential software customers. As part of its sales of customized software, petitioner supplied its customers, when appropriate, with the computer equipment to run the customized software. Petitioner's president testified that petitioner purchased computer hardware from IBM and other manufacturers, added the customized software and then resold the hardware with the customized software to its customers. As the Administrative Law Judge noted, petitioner's witnesses consistently spoke of these transactions as purchases by VIP and resales to its customers. While employees of the computer manufacturers installed the equipment on the customer's premises, petitioner set the price for the equipment, and billed its customers for the equipment and the costs of installation. These billing procedures further establish that these were petitioner's sales and not sales by the computer manufacturer. Thus, the Administrative Law Judge correctly concluded that petitioner sold tangible personal property in the State and that such sales were a result of petitioner's solicitation making petitioner a vendor under former Tax Law § 1101(b)(8)(i)(C).

Having determined that petitioner met the State's statutory definition of a vendor required to collect the use tax on items taxed by Article 28, we must now determine whether petitioner's activities satisfied the nexus requirement of the Commerce Clause of the United States Constitution.[4] Petitioner asserts that its

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[4] A state may have authority to tax under the Due Process clause of the Constitution as only a minimal connection with the state is required; however, the imposition of the tax may still violate the Commerce Clause because the potential taxpayer's contacts with the state are insufficient to establish nexus (*Quill Corp. v. North Dakota*, _____ US

contacts with New York State are insufficient to warrant the imposition of tax collection responsibilities.

Where a vendor's activities in the State consist solely of solicitation of customer sales and shipment of goods by mail or common carrier, the vendor's contacts with the state are insufficient to constitute nexus and an obligation to collect a state's use tax cannot be imposed on the vendor by the state (*Quill Corp. v. North Dakota*, ___ US ___, 112 S Ct 1904; *National Bellas Hess v. Department of Rev. of State of Illinois*, 386 US 753). A vendor must have a physical presence in a state before the state can impose the obligation to collect use taxes (*Quill Corp. v. North Dakota, supra*; *National Geographic Socy. v. California Bd. of Equalization*, 430 US 551; *National Bellas Hess v. Department of Rev. of State of Illinois, supra*). To date, the Court has not quantified the extent of the physical presence needed to impose such an obligation. The Court has stated, however, that the existence of a "slightest presence" within the state is not enough (*Quill Corp. v. North Dakota, supra*; 112 S Ct 1904, 1915, footnote 8; *National Geographic Socy. v. California Bd. of Equalization, supra*, at 556).

In *Quill*, the court acknowledged that the point at which nexus is found to exist is an artificial point (*Quill Corp. v. North Dakota, supra*, 112 S Ct 1904, 1914). To determine if this artificial point has been reached, a careful evaluation of the vendor's activities is required, for "[t]he test is simply the nature and extent of the activities of the [vendor] in [the state]" (*Scripto, Inc. v. Carson*, 362 US 207, 211-212; *see also, Felt & Tarrant Mfg. Co. v. Gallagher*, 306 US 62 [where, as in *Scripto*, the Court examined the activities of the vendor's salesmen and found them to establish sufficient nexus to justify imposition of use tax liability]; *Matter of Orvis, Inc.*, Tax Appeals Tribunal, January 14, 1993).

____, 112 S Ct 1904). Since we find that in this case, the Commerce Clause requirements have been met, it is unnecessary for us to separately discuss the application of the Due Process Clause.

The Court's decision in *National Geographic* is instructive as to what activities or factors should be considered in determining whether a taxpayer's presence surpasses that of a "slight physical presence." The National Geographic Society conducted an out-of-state mail order business and at the same time maintained two small offices in California that solicited advertisements for National Geographic Magazine. California sought to impose use tax obligations on the Society for its mail order sales based upon the presence of the California offices. The Society argued that the business activities of these offices were totally unrelated to the mail order sales that California sought to tax and, therefore, the Court should not take the activities of the in-state offices into account in determining whether sufficient nexus exited. This argument was specifically rejected by the Court (*National Geographic Socy. v. California Bd. of Equalization*, *supra*, at 652). The Court stated that for nexus to exist there is no requirement that, in addition to a relationship between the taxing state and the taxpayer, there be a direct correlation between the activity sought to be taxed and the taxpayer's activity in the state (*National Geographic Socy. v. California Bd. of Equalization*, *supra*, at 560). In determining whether nexus exists, the Court indicated that it is the seller's activities of whatever nature in the state which must be examined (*National Geographic Socy. v. California Bd. of Equalization*, *supra*, at 560). While the Court did not define at what point the Society's activities surpassed a "slightest presence," it did hold "that [National Geographic's] maintenance of the two offices in California and activities there adequately establish[ed] a relationship or 'nexus' between the Society and the State that render[ed] constitutional the obligations imposed upon [National Geographic] pursuant to §§ 6203 and 6204 [of the California Tax Law]" (*National Geographic Socy. v. California Bd. of Equalization*, *supra*, at 556). The Court found that the Society was subject to the California use tax because sufficient nexus existed and the Society met the statutory definition of a "retailer engaged in business in [the] state (*National Geographic Socy. v. California Bd. of Equalization*, *supra*, at 556).

Petitioner makes the same argument made by the Society asserting that, in determining if sufficient nexus exists, only in-state activities associated with taxable sales are to be examined and that, since its physical presence in the State was only related to its nontaxable sales of computer software, insufficient nexus exists. We agree with the Administrative Law Judge that, based upon the decision in *National Geographic*, "all of [petitioner's] activities in New York may properly be considered in determining whether [the petitioner] had a sufficient connection with New York to warrant imposition of the burden to collect the use tax" (Determination, Conclusion of Law "D").

In our view, petitioner's activities represent more than a "slight physical presence" in this State. While petitioner's activities in the State may be less substantial than those in *National Geographic*, we think that the "nature and extent of the activities" (*Scripto, Inc. v. Carson, supra*, at 211) of petitioner's employees in New York created a sufficient nexus to impose a use tax liability for the sale of the computer hardware. Petitioner's employees periodically entered New York to install or to provide maintenance for the customized computer software it sold.[5] The computer equipment on which the customized software was installed was either previously owned by petitioner's customers or newly purchased from petitioner in order to make use of petitioner's customized software packages. We have previously discussed that petitioner's sales of the computer hardware and software resulted from petitioner's solicitation in the State. Petitioner is, therefore, subject to the requirements of Article 28 of the Tax Law as its solicitation of customers and sales of tangible personal property qualified petitioner as a vendor under Tax Law § 1101(b)(8)(i)(C), and petitioner's physical presence by its employees installing and maintaining the computer software sold to New York customers created sufficient nexus.

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[5] Petitioner's employees also made occasional visits into the State to hold training sessions on the use of its software programs.

On the issue of penalties, petitioner has made the same arguments on exception that it made before the Administrative Law Judge. We find no reason to alter the Administrative Law Judge's determination and, therefore, for the reasons stated in that determination, we uphold the Administrative Law Judge's determination that petitioner has not established reasonable cause for the abatement of penalties.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioner Vermont Information Processing, Inc. is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petition of Vermont Information Processing, Inc. is denied; and

4. The Notice of Determination issued to petitioner Vermont Information Processing, Inc. on November 27, 1987 is sustained.

DATED: Troy, New York

[Jan. 21, 1993]

/s/ John P. Dugan
John P. Dugan
President

/s/ Francis R. Koenig
Francis R. Koenig
Commissioner

/s/ Marie T. Jones
Marie T. Jones
Commissioner

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition
of
VERMONT INFORMATION
PROCESSING, INC.

DETERMINATION
DTA No. 806207

for Revision of a Determination or for
Refund of Sales and Use Taxes under Articles
28 and 29 of the Tax Law for the Period
December 1, 1983 through November 30, 1986.

Petitioner Vermont Information Processing, Inc., P.O. Box 470, Hercules Drive, Colchester, Vermont 05446 filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1983 through November 30, 1986.

A hearing was held before Jean Corigliano, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on June 10, 1991 at 1:15 P.M. Petitioner filed a brief on August 9, 1991. The Division of Taxation filed a brief on October 18, 1991, and petitioner filed a reply on October 29, 1991. Petitioner appeared by James H. Tully, Jr., Esq. The Division of Taxation appeared by William F. Collins, Esq. (Gary Palmer, Esq., of counsel).

ISSUES

I. Whether petitioner was a vendor as defined by Tax Law § 1101(b)(8) and thereby required to collect the taxes imposed under Article 28 of the Tax Law.

II. Whether, if petitioner was a vendor pursuant to the Tax Law, the United States Constitution prevents New York from

imposing a duty upon petitioner to collect the use tax imposed under section 1110 of the Tax Law.

III. Whether petitioner has established reasonable cause for its failure to collect and remit the use tax.

FINDINGS OF FACT

1. On November 27, 1987, the Division of Taxation ("Division") issued to petitioner, Vermont Information Processing, Inc. ("VIP"), a Notice of Determination and Demand for Payment of Sales and Use Taxes Due for the period December 1, 1983 through November 30, 1986, assessing tax of $513,112.11 plus penalty and interest.

2. VIP is a Vermont corporation which produces and sells computer software to beverage distributors throughout the United States. During an audit of a beverage distributor located in Troy, New York, an auditor discovered a letter on VIP letterhead which indicated that VIP was making sales in New York State. As a result, the Division commenced an audit of VIP.

3. VIP was not registered to collect sales and use taxes on behalf of New York State. At the time of the audit, VIP contended that it was not required to register and had no duty to collect New York taxes. On that basis, it refused the Division access to its records. The Division obtained copies of VIP's Federal and Vermont income tax returns and used information from those returns to estimate New York taxable sales for the audit period of $7,330,173.00, with a use tax due on that amount of $512,112.11.

4. Following a conciliation conference, VIP agreed to allow the auditors to examine its records for the period December 1, 1983 through November 30, 1986. The VIP sales invoices inspected by the Division showed charges for computer hardware, charges for maintenance and installation of that hardware, charges for "site days" (days spent on the customer's business premises), travel expenses, charges for software systems and charges for the installation and maintenance of the software. The Division determined that receipts from the sale and maintenance of the

software were not subject to sales or use tax. Charges associated with the sale, maintenance and installation of computer hardware were deemed to be subject to tax. Reimbursements for travel expenses incurred by VIP in connection with service provided to New York customers and charges for site days (days spent at the customer's location) were not deemed taxable by New York. The Division's review of the invoices resulted in a determination of taxable sales of $1,216,744.00. In accordance with this determination, the Division issued a conciliation order, dated September 30, 1988, reducing the tax due to $85,172.08 and sustaining the imposition of penalty. Before hearing, the Division agreed to reduce the amount of tax asserted to $73,275.04.

5. It is VIP's position that it had no duty to collect and remit New York State sales or use tax, and it challenges the assessment on that basis alone. It concedes that if it is finally determined that VIP was under a duty to collect the tax the amount of tax due for the audit period is $73,275.04.

6. VIP operates its business from its headquarters in Colchester, Vermont. It does not maintain a place of business in New York. During the audit period, it employed between 20 to 30 workers. Two or three employees were engaged in accounting and bookkeeping operations. Harold Aiken, the president of VIP, and another employee were involved in sales. Approximately four employees were identified as installers. Workers in these positions gathered information from customers regarding the customer's computer system, recordkeeping and business operations. The installers (essentially computer programmers) then adapted VIP computer software to the needs of the customer. The installers also were involved in training the customers to operate the VIP programs. VIP also employed two trainers and approximately four people to answer questions from customers by telephone.

7. VIP had no employees in New York and did not employ salesmen to travel into New York to solicit sales, nor did it advertise in New York newspapers or periodicals or engage in direct mail solicitation. Most of its potential customers heard

about VIP through word of mouth and contacted VIP to learn more about its product. VIP representatives spoke to potential customers over the telephone and mailed them brochures describing VIP's products and services. Interested parties were invited to Vermont for a demonstration or encouraged to view an operating VIP system at the workplace of an existing VIP custom in New York.

8. If a beverage distributor decided to purchase VIP's services, the distributor was sent a contract by United Parcel Service ("UPS"). After execution of the contract, the customer was asked to complete a variety of forms which provided VIP with information regarding the customer's business operations and recordkeeping systems. The information supplied by the customer was used by VIP to create software suitable for that customer's particular business operations.

9. If a customer already possessed a viable computer system, VIP sold only the software programs and VIP's services. If a customer did not already own a computer, VIP would attempt to sell it computer hardware as well. VIP was an industry marketer, authorized by IBM to sell IBM computers to beverage distributors. Mr. Aiken described VIP's relationship with IBM as follows:

> Mr. Aiken: "They [IBM] ship equipment to me, they allow me to have 10 or 15 days credit on the equipment, and then I resell it, but I can only resell it to beverage distributors. They do all installation shippings as if it were sold by their regular representative who might be in Los Angeles. They maintain it by their own maintenance people, and the only thing I'm really doing is adding value to it, and I'm putting my software on it, setting the customer on it, training them, providing him on a hotline service afterward and an ongoing thing for years and years."
>
> Administrative law judge: "Does your customer have any separate contract with IBM for maintenance, for guarantees or warranties?"

Mr. Aiken: "He would have. The agreement we would have him sign is an IBM agreement, it is not a VIP agreement.... We submit the paperwork so it doesn't get lost or messed up, and he is covered under maintenance by IBM."

Administrative law judge: "And would you separately charge on your invoice for any of that?"

Mr. Aiken: "No." (Hearing Tr., pp. 76-77.)

10. VIP also sold computer hardware manufactured by a company named MSI and a third company. Its relationship with those companies was similar to its relationship with IBM.

11. If a VIP transaction included the purchase of computer hardware, the computer was mailed directly to VIP where the software was loaded, and the computer was then shipped by VIP to the customer, via common carrier. If the customer purchased only software, the program was placed on a disk which was shipped to the customer via common carrier.

12. VIP's customers were usually trained to use the programs developed for them at VIP's headquarters in Vermont. As part of its services, VIP personnel were available to VIP customers by telephone to answer questions and resolve any problems the customer might be having with the VIP computer program. In addition, VIP installers were able to directly access a customer's computer from VIP's own computer system in Vermont through the use of a modem. A customer's computer program could be modified or corrected in this fashion, without the VIP employee leaving Vermont.

13. VIP personnel did not routinely travel to their customers' locales to answer questions or service customer needs. In fact, it was VIP's policy to discourage travel as much as possible. However, VIP did travel to the customer's place of business if absolutely necessary to install or maintain software or handle problems the customer was having with the software. Mr. Aiken estimated that approximately five percent of its customer accounts required some travel.

14. VIP sold its customers on-going services, such as updating the computer programs, for which it charged a monthly fee. VIP used the terms "maintenance" and "installation" to refer to services connected with the software programs; however, VIP did not install or maintain computer hardware or send its employees to its customer's facilities for the purpose of maintaining or installing such hardware. As Mr. Aiken stated in his testimony: "When we call it installation time, that's like you and I talking, it is hours, it is not — I don't have a guy that uses a screwdriver. I don't have that" (transcript at 64). Any computer hardware sold by VIP was installed, serviced and maintained at the customer's business location by employees of the hardware manufacturer.

15. During the course of the audit, the Division obtained a variety of information which led it to believe that VIP was entering New York to install both hardware and software at its customers' business locations and that VIP entered New York to conduct training sessions. That information consisted of a letter on VIP letterhead, VIP sales invoices, and conversations with VIP customers. Since VIP vigorously disputes the meaning and importance attributed by the Division to this information, it is necessary to review it in some detail.

(a) The Division introduced a letter dated February 13, 1985 from VIP to a Troy, New York customer. As material here, the letter summarizes computer hardware and software purchased by the customer and contains the following statements:

"PAYMENT SCHEDULE:

Due with this letter (hardware deposit 10%) (received)	3,447.90
Due at installation (hardware 90% + software)	36,481.00

You should budget one to two days at $60.00 per hour for training and installation on the computer and software, as well as actual per diem expenses. Any applicable sales, use, or excise taxes are your responsibility and should be paid to the proper authorities. All VIP charges will be billed when performed.

> If John J. Bolond Dist. and VIP determine that an installer is needed on-site for additional data prep within 60 days of installation, VIP will provide that person at no charge to John J. Boland Dist."

The letter also states separate charges for the maintenance of the hardware and software.

An auditor spoke with a representative of the Troy beverage distributor. When asked the substance of that conversation the auditor stated: "They said that the representative installed the computer and trained them and that they had a seminar in Albany in March of 1987." (Transcript at 33.)

The auditor believed that the letter provided evidence that VIP entered New York for installation and maintenance of computer hardware and training.

(b) The second document relied on by the Division was a VIP sales invoice to a customer in Athens, New York. The customer was charged for VIP travel time and expenses and for training. The invoice does not indicate where the training took place.

(c) Two other invoices to separate New York customers show charges for software, hardware, hardware maintenance, and "PC/Set Up/Test."[1]

(d) Three invoices to a Plattsburgh customer show miscellaneous travel and transportation expenses and charges for "installation." An auditor spoke with an employee of the Plattsburgh customer and was told that a VIP employee went to the business offices in Plattsburgh to "install system and train him" in its use (Exhibit M, notation made by auditor).

(e) An invoice to an Ithaca, New York company shows the sale of hardware and software by VIP.

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[1] In his testimony, Mr. Aiken explained this as a charge "to set up a diskette" (Transcript at 59).

16. When reviewing the VIP invoices, the auditor made a listing of each invoice which she believed demonstrated VIP's presence in New York in connection with its sales of computer hardware and software in New York. The listing provides the following information for each such invoice: the customer name, the invoice date, the invoice number, the total invoice amount, the amount taxable by New York State, and comments. The comments section identifies those items on the invoice which the auditor construed as evidencing VIP's presence in New York. These items can be separated into two general categories: (1) items of travel expense or charges for site visits and (2) items connected with the installation or maintenance of either computer hardware or software. Approximately 41 invoices contain items in the first category. The remaining 40 invoices show charges for items related to installation and maintenance of computer hardware or software. There is no correlation between the hardware installation charges and the travel or site visit charges. For example, invoice number 121188 showed a $480.00 charge for installation of hardware. The auditor included the invoice in the listing of invoices showing a New York presence, presumably because she believed that a VIP employee traveled into New York to install the hardware. The comments section does not indicate that there was a charge for travel expenses, and there is not a separate invoice for travel expenses which can be correlated to the installation found on invoice number 121188. There are some instances where a charge for installation of software is found on the same invoice as a travel expense charge. Invoice number 730 showed an invoice amount of $149.01 for transportation, room, meals and PC installation. None of this was deemed taxable. The invoices do not undermine the credibility of Mr. Aiken's testimony that VIP did not travel to New York to install, service or maintain computer hardware.

17. After receiving access to VIP's records, the auditor listed all invoices showing sales of property or services subject to sales or use taxes. Her worksheets list approximately 154 such invoices for the audit period.

18. Mr. Aiken attended a seminar in New York. The subject of the seminar was New York's bottle bill. Mr. Aiken participated as a presenter at the invitation of the seminar's sponsors. The seminar was not conducted for the purpose of training VIP customers or to solicit business in New York, and it occurred after the expiration of the audit period.

19. VIP registered to do business in New York with the Department of State over 10 years ago. On advice from an attorney, VIP ended its registration. VIP also consulted an accountant about 10 years ago who advised VIP that it had no duty to register as a vendor in New York State or to collect New State use tax.

CONCLUSIONS OF LAW

A. Section 1110 of the Tax Law imposes upon all persons a compensating use tax for use within New York State of any tangible personal property purchased at retail, except to the extent that such property has already been subject to sales tax. The obligation to collect the use tax is imposed upon every vendor of tangible personal property (Tax Law § 1131[1]). Pursuant to Tax Law former § 1101(b)(8)(i),[2] in effect during the audit period, a vendor includes:

"(A) A person making sales of tangible personal property or services, the receipts from which are taxed by [article 28];

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[2] Effective September 1, 1989, the statutory definition of vendor was modified. Tax Law § 1101(b)(8)(i)(C) now defines a vendor, in pertinent part, as:

"A person who solicits business . . .

(II) by distribution of catalogs or other advertising matter, without regard to whether such distribution is the result of regular or systematic solicitation, if such person has some additional connection with the state which satisfies the nexus requirement of the United States constitution; and by reason thereof makes sales to persons within the state of tangible personal property or services, the use of which is taxed by this article."

(B) A person maintaining a place of business in the state and making sales, whether at such place of business or elsewhere, to persons within the state of tangible personal property or services, the use of which is taxed by [article 28];

(C) A person who solicits business either by employees, independent contractors, agents or other representatives or by distribution of catalogues or other advertising matter and by reason thereof makes sales to persons within the state of tangible personal property or services, the use of which is taxed by this article".

The Division premised its finding that VIP is a vendor and liable for collection of use tax on two grounds. First, the Division found that petitioner made sales of tangible personal property (computer hardware) in New York. Second, the Division found that VIP employees traveled to New York to perform services subject to tax under Tax Law § 1105(c)(3), specifically to install, maintain and service the computer hardware.

Petitioner denies that it sold tangible personal property in New York and contends that its employees entered New York only in connection with the servicing of computer software. Even if it did make sales of tangible personal property in New York, petitioner claims that the State cannot burden it with a duty to collect use tax because it lacks the nexus with New York required by the Commerce Clause and the Due Process Clause of the United States Constitution. In order to determine whether petitioner was a vendor under the Tax Law and to resolve the nexus issue, it is first necessary to determine the nature and extent of VIP's activities in New York as established by the evidence in the record.

B. The Division placed sufficient evidence in the record to establish that it had a reasonable basis for concluding the VIP sold tangible personal property in New York and entered New York to install and maintain that property. That evidence consisted of the letters and invoices obtained by the auditor during her audit and the auditor's conversations with two VIP customers.

Moreover, the auditor's analysis of invoices reviewed after the conciliation conference lent support to the Division's position. Accordingly, the burden was upon VIP to show by clear and convincing evidence that it did not sell tangible personal property in New York or enter New York to perform services taxable under article 28 (*Matter of Sarantopoulos*, Tax Appeals Tribunal, February 28, 1991).

C. Petitioner failed to prove that it did not sell tangible personal property in New York. VIP solicited sales in New York and by reason of that solicitation made sales of tangible personal property (computer hardware) within New York. VIP argued that the computer manufacturers, not VIP, were the actual sellers of the hardware, but the evidence establishes otherwise. In fact, VIP's witnesses consistently spoke of these transactions in terms of a purchase by VIP and a resale to VIP's customers (*see, e.g.*, the testimony of Harold Aiken in Finding of Fact "9"). VIP's contention that it did not solicit business in New York is also rejected. VIP sent brochures to potential customers in New York, negotiated sales over the telephone, and arranged for potential customers to see VIP computer systems demonstrated either in New York or Vermont. These activities constitute solicitation of business, and by reason of such solicitation VIP made sales of tangible personal property in New York. This activity alone establishes that VIP was a vendor under section 1101(b)(8)(i)(A), (C) of the Tax Law.

Petitioner proved that it performed no services in New York subject to taxation under article 28. There is no question that VIP employees traveled into New York to install computer software, solve problems related to its use and provide training; however, VIP offered the credible testimony of its president and comptroller to establish that VIP did not install, service or maintain computer hardware in New York. Their testimony established that the auditor misapprehended information shown on the invoices and letters she viewed. The confusion was caused, in part, by VIP's practice of referring to services related to the computer software as "installation". A statement on an invoice showing, for example, "PC installation" referred to the placing

of a computer program on a disk, an activity that normally occurred in Vermont. The listing of invoices made by the auditor provides no evidence that VIP employees entered New York to install or service computer hardware. Although the listing shows charges related to the hardware and charges for travel or site days, there is never any correlation between the two; that is, the invoices never show a charge for travel expenses that can be directly related to a charge for hardware installation. Thus, the invoices themselves lend credibility to the testimony of VIP's witnesses.

In its brief, the Division states: "If the content of the actual invoices differ [sic] materially from the auditor's transcription, it was the petitioner's burden to produce these records in support of its position" (Division's Brief at 4). The point here is not that the auditor did not accurately transcribe information but that she misinterpreted it. There is no independent evidence in the record that supports the auditor's interpretation, except the hearsay statements of two VIP customers (*see* Finding of Facts "15[a]" and "15[d]"). The statements themselves are ambiguous and do not clearly indicate whether the speakers were referring to the installation of computer hardware or software. Moreover, they were related by the auditor who understood the term "installation" to refer to hardware. When contrasted with the testimony of VIP's witnesses, given under oath and subject to cross-examination, those statements can carry little weight. In sum, the evidence shows that VIP employees entered New York only to service and maintain the computer software and to provide training in its use. These are not services subject to tax under article 28.

The Division determined that the receipts from VIP's computer programs and software sales were not subject to tax under article 28 because the programs were adapted and modified for each individual customer's use. Computer programs of this nature are deemed to be intangible personal property, whether directly entered into the computer or placed on disks, tapes, or transmitted by another medium (*see*, *Matter of Economic Information Systems*, State Tax Commission, May 26, 1987 [TSB-H-

87(218)S]). As an intangible product, such software does not fall within the scope of article 28. Services rendered in connection with the intangible personal property likewise are not subject to the tax imposed under article 28. Thus, VIP would not have been required to register as a vendor or to collect use tax if its *only* sales transactions involved the creation and servicing of the computer software, even if it maintained a place of business in New York.

The Division argues that it is of no significance that VIP employees serviced only the software, since the software and hardware function as a unit. It may be true that one cannot create or modify a computer program without using a computer. However, the Division itself distinguishes between software and hardware, deeming the former to be intangible personal property not subject to sales or use tax (*see*, *Answer Systems, Inc.*, Advisory Opinion, January 5, 1991 [TSB-A-91(9)S]). More importantly, the Division recognizes that the services of creating, updating and modifying the software are not taxable by article 28 even where the data or programs are "entered into a computer directly" (Department of Taxation, Technical Services Bulletin 1978-[S]; *see also*, *Answer Systems*, *supra*). Based on the fact that VIP only provided services in connection with the computer software, it is concluded that it performed no services in New York subject to New York's sales and use tax.[3]

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[3] The Technical Services Bulletin cited indicates that compute software of a certain nature is "exempt" from sales tax. In fact, the Tax Law does not provide a statutory exemption for software of any kind. Because software (of the kind under discussion) is deemed to be intangible personal property, the receipts from sale of the software are not taxed by article 28. Inasmuch as such receipts do not fall within the scope of article 28, a person whose activities are confined to the selling of such software is not a vendor as defined by section 1101(b)(8) (*cf. Matter of Felix Industries*, Tax Appeals Tribunal, August 22, 1991 [where the Tribunal held that a vendor is not free from the duty to register because his sales, otherwise taxable under article 28, were exempted from sales tax by specific provisions of the Tax Law]).

Nonetheless, the evidence is sufficient to establish that under section 1101(b)(8)(i)(A), (C) VIP was a vendor during the audit period because it sold tangible personal property in New York.

D. The conclusion that VIP was a vendor under the Tax Law does not settle the issues raised here however. Past United States Supreme Court decisions have recognized a constitutional limitation upon a state's power to require an out-of-state seller to collect use tax (*see, National Bellas Hess v. Department of Revenue*, 386 US 753, 87 S Ct 1389, 18 L Ed 2d 505). Those constitutional limitations are reflected in the Rules and Regulations of the Commissioner of Taxation and Finance, in effect during the audit period. 20 NYCRR former 526.10(e)(2) limits the definition of a vendor, stating:

> "A person making sales to his customers within the State, who has solicited such sales by the interstate distribution of catalogs or other advertising material by mail and who delivers the merchandise through the mail or by common carrier, and who neither maintains a place of business as defined in subdivision (c) of this section, nor solicits business as defined in subdivision (d) of this section, is not required to register as a vendor."

A person is deemed to be soliciting business for purposes of the regulation if he has employees, salesmen, independent contractors or other agents soliciting potential customers in New York (20 NYCRR former 526.10[d][1]).

Quite clearly, if VIP's sales of tangible personal property in New York involved only the solicitation of sales of the computer hardware by mail and telephone and the delivery of that merchandise by common carrier, VIP would not be deemed to be a vendor under the regulation and thus would not be responsible for the collection of use tax. The issue then is whether VIP's sales of tangible personal property in New York coupled with its presence in New York to perform services *not* taxed by article 28 creates the requisite nexus which would allow New York to require VIP to collect the use tax. VIP claims that the activities it carried on in New York are insufficient to create a nexus between VIP and New York because the receipts from those

activities were not subject to sales tax and because the activities were irregular and few in number.

The opinion of the Supreme Court in *National Geographic Society v. California Board of Equalization* (430 US 551, 51 L Ed 2d 631) is especially instructive in resolving the former issue. The appellant, a not-for-profit corporation, maintained two offices in California that solicited advertising for the Society's magazine but had no connection to the Society's mail order business conducted from its headquarters in the District of Columbia. The California Supreme Court had concluded that the "slightest presence" of the seller in California established sufficient nexus between the State and the seller to support the imposition of the duty to collect use tax. The Society argued:

> "[t]hat there must exist a relationship not only between the seller and the taxing State, but also between the activity of the seller sought to be taxed and the seller's activity within the State" (*id* at 560, 51 L Ed 2d 631, 639).

The Court rejected both approaches. It surveyed the decisions in this area and concluded that:

> "[t]he relevant constitutional test to establish the requisite nexus for requiring an out-of-state seller to collect and pay the use tax is not whether the duty to collect the use tax relates to the seller's activities within the State, but simply whether the facts demonstrate 'some definite link, some minimum connection between [the State and] the *person*...it seeks to tax'." (*Id*, at 561, 51 L Ed 2d 631, 640, quoting *Miller Bros. v. Maryland*, 347 US 340, 74 S Ct 535, 539: emphasis added in *National Geographic*.)

Based on the decision in *National Geographic*, it is concluded that all of VIP's activities in New York may properly be considered in determining whether VIP had a sufficient connection with New York to warrant imposition of the burden to collect use tax. A sufficient nexus has been found to exist where local agents of the seller were present in the State and operated out of premises paid for by the seller (*Felt & Tarrant Mfg. Co.*

v. Gallagher, 306 US 62, 83 L Ed 2d 488). A state may impose the tax burden on a company maintaining retail stores in the state even if the retail stores are not directly involved in the company's out-of-state mail order business (*Nelson v. Sears, Roebuck & Co.*, 312 US 359, 85 L Ed 868). In *National Geographic*, the Court held that the Society's offices in California created sufficient nexus to subject the Society to use tax liability, although the offices had no direct relationship to the seller's mail order business (*National Geographic Society v. California Board of Equalization, supra*).

VIP's activities in New York are somewhat less substantial than those described in the cited cases. VIP does not own or lease property in New York, it does not have a telephone in New York, and it has no employees or agents in New York. Nonetheless, its activities in New York are more extensive than those of the mail-order company described in *Bellas Hess*. In determining exactly how much activity and what kind of activity is necessary to create a nexus between the State and the person it wishes to subject to use tax liability, the Supreme Court's examination in *National Geographic* of the *Bellas Hess* opinion is notable. The Court stated:

> "*National Bellas Hess, Inc. v. Illinois Rev. Dept*, (citations omitted) presented the question [of nexus] in the case of an out-of-state seller whose *only* connection with customers in the taxing State was by common carrier or mail. Illinois subjected appellant Bellas Hess, a national mail-order house centered in Missouri, to use tax liability based upon mail-order sales to customers in that State. Bellas Hess owned no tangible property in Illinois, had no sales outlets, representatives, telephone listings, or solicitors in that State, and did not advertise there by radio, television, billboards, or newspapers. It communicated with potential customers by mailing catalogues throughout the United States including Illinois, twice a year and occasionally supplemented this effort by mailing out 'flyers'. All orders for merchandise were mailed to Bellas Hess' Missouri plant, and the goods were sent to customers by mail or common carrier. *Bellas Hess* held that, constitutionally, the basis for the requisite

nexus was not to be found *solely* in Bellas Hess' mail-order activities in the State. The Court's opinion carefully underscored, however, the 'sharp distinction...between mail order sellers with retail outlets, solicitors, or property within [the taxing] State, and those [like Bellas Hess] who do no more than communicate with customers in the State or by mail or common carrier as part of a general interstate business.'" (*National Geographic Society v. State Board of Equalization*, *supra* at 559, 51 L Ed 2d 631, 639, quoting *Bellas Hess v. Illinois Rev. Dept.*, *supra* at 1392; emphasis added.)

The Court made one other observation pertinent to this determination. It noted that the only burden placed on the out-of-state seller by the compensating use tax is an administrative one of collecting and remitting the tax. The out-of-state seller becomes liable for the tax only if it fails or refuses to collect it from consumers whose "identification as a resident of the taxing State is self-evident" (*id.* at 558, 51 L Ed 631, 639).

VIP conducted a substantial amount of business activity in New York. Its sales of taxable items amounted to $1,216,744.00 during the audit period. In addition, it had sales of nontaxable goods and services in an undetermined amount. Undoubtedly, its sales in New York were increased and enhanced by its activities in New York. It was able to promise its potential customers that an installer would visit New York to solve any problems with the systems purchased (Finding of Fact "15[a]"). VIP systems operating at the offices of existing customers in New York were used to demonstrate the VIP product to potential New York customers (Finding of Fact "7"). VIP communicated regularly with existing new York customers over telephone lines, either in the traditional manner or by computer linkage (Finding of Fact "12"). Petitioner claims that the actual number of times its employees visited New York were too infrequent to create a definite link between New York and VIP. The VIP invoices show approximately 41 trips into New York during the audit period based upon charges to its customers for site days and travel expenses (Finding of Fact "6"), and the auditor's workpapers show approximately 154 taxable transactions in New

York during the same period. Thus, the actual number of times a VIP employee visited New York is not insignificant in relationship to its sales in New York. More importantly, these visits to New York were significantly connected with VIP's ability to establish and maintain a market for the computer hardware and software it sold in New York. Therefore, it is concluded that VIP's presence in New York through its installers' visits to this State created a sufficient nexus between New York and VIP to subject VIP to use tax liability.

E. Petitioner seeks abatement of penalties on the ground that it had reasonable cause for believing that it was not liable for use taxes. Petitioner contends that reasonable cause is shown by the following facts: (1) petitioner's primary business is the creation of software which is an activity not subject to tax under article 28; (2) petitioner informed its customers that they were responsible for payment of any taxes due; (3) petitioner believed that IBM was collecting and remitting sales taxes on sales in New York State; (4) petitioner maintained no offices or employees in New York and did not advertise in New York; (4) petitioner consulted an accounting firm which advised it that it had no use tax liability in New York. At hearing, petitioner's attorney argued that this case is one of first impression and that "if nexus is determined in this case it will be as far as the State of New York has ever gotten" (transcript at 87). He argued that a penalty should not be imposed on petitioner in such a case.

Petitioner was assessed penalty under section 1145(a)(1)(i) of the Tax Law which provides for imposition of penalty whenever any person fails "to file a return or pay over any tax...within the time required by or pursuant to [article 28]". Section 1145(a)(1)(iii) allows for abatement of penalty where the petitioner has established that such failure was due to reasonable cause and not due to willful neglect. The taxpayer bears the burden of establishing reasonable cause as well as the absence of willful neglect (*see, e.g., Matter of T.V. Date, Inc.*, Tax Appeals Tribunal, March 2, 1989).

In determining whether reasonable cause exists, an important factor to consider is the extent of the taxpayer's efforts to ascertain its tax liability (*see Matter of John Grace & Co.*, Tax Appeals Tribunal, May 9, 1990; *see also*, 20 NYCRR 536.5[d][1], [2]). Reliance on the advice of a tax professional is not necessarily grounds to support a finding of reasonable cause (*Matter of Auerbach v. State Tax Commn.*, 142 AD2d 390, 536 NYS2d 557). Here, there was testimony that petitioner consulted with an accounting firm and was advised that it had no use tax liability. However, there was no evidence to show exactly what facts were presented to the tax advisor or to establish the nature and extent of the inquiry made and advice given by the advisor. The cancellation of penalties on the basis of the mere allegation that an accountant's advice was sought would eviscerate the penalty provisions altogether (*see, Matter of LT & B Realty v. State Tax Comm.*, 141 AD2d 185, 535 NYS2d 121, 123).

Petitioner's contention that it believed that either IBM or its customers were remitting any sales taxes that might be due to New York tends to demonstrate willful neglect rather than reasonable cause. A vendor cannot delegate its statutory duty to collect and remit tax. Petitioner's reliance on others, who also may have had a duty to pay tax, does not demonstrate that petitioner made a good faith effort to ascertain its own tax liability.

Finally, the fact that New York's courts have not ruled on a case presenting the same set of facts as those presented here is not a sufficient basis to establish reasonable cause.[4] In order to establish reasonable cause, the taxpayer must show that he acted with ordinary business care and prudence in attempting to ascertain his tax liability (*Matter of A & V Crown*, Tax Appeals

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[4] This determination is based on the law that existed during the audit period. There is no attempt here to restrict nexus requirements or to anticipate future Supreme Court decisions (*see, e.g., Heitkamp v. Quill Corp.*, 470 NW2d 203, *cert granted* ___ vs ___, 112 S Ct 49, 116 L Ed 2d 27).

Tribunal, May 24, 1990; *see also*, 20 NYCRR 536.5[d][2]). There is no such showing here. For example, petitioner did not contact the Division to ask its interpretation of the law or seek an advisory opinion of the Commissioner. In the absence of such inquiries, petitioner failed to prove that its actions did not constitute willful neglect.

F. The petition of Vermont Information Processing, Inc. is denied and the Notice of Determination and Demand for Payment of Sales and Use Taxes as modified by agreement of the parties (Findings of Fact "4" and "5") is sustained.

DATED: Troy, New York

[FEB. 27, 1992]

/s/ Jean Corigliano
ADMINISTRATIVE LAW JUDGE